
SEC to Crack Down on Misleading ESG Claims With Fund Rules.

- **Agency seeks to eliminate names that critics call greenwashing**
- **Wall Street regulator proposed plan at meeting on Wednesday**

The US Securities and Exchange Commission is taking its biggest step yet to stop money managers from misleading investors when they claim their funds are focused on environmental, social or governance issues.

The agency proposed a slate of new restrictions Wednesday aimed at ensuring ESG funds accurately describe their investments. Some would also need to disclose the aggregated greenhouse gas emissions of companies they're invested in, according to the SEC.

Concerns are mounting over a lack of consistent standards for investments claiming to be sustainable, with the ESG label slapped on everything from exchange-traded funds to complex derivatives. During the Biden administration, the SEC has been focused on the issue, and has signaled a clampdown was looming.

"It is important that investors have consistent and comparable disclosures about asset managers' ESG strategies so they can understand what data underlies funds' claims and choose the right investments for them," SEC Chair Gary Gensler said in a statement.

In one proposed change, the SEC would expand an existing rule to ensure funds labeled ESG invest at least 80% of their assets in a way that lines up with that strategy.

The agency is also weighing more standardized disclosures about their investment strategies. Those changes could help investors get a better understanding of the underlying investments in a fund and its overall strategy for addressing climate change or social issues like diversity, equity and inclusion.

Republicans oppose the SEC's focus on ESG, and say the agency shouldn't play a role in rating municipal debt and or in making decisions about provide financing to oil, gas and coal companies.

"These proposals are designed to manufacture activism by funds on ESG issues," said Republican Commissioner Hester Peirce, who opposed the proposal.

In a separate move, the SEC announced on Monday that Bank of New York Mellon Corp. unit agreed to pay $1.5 million to settle claims that it falsely implied some mutual funds had undergone an ESG quality review. BNY, which didn't admit or deny the allegations, said that it had taken steps to improve communications with investors.

Globally, some $2.7 trillion is parked in ESG-labeled exchange-traded funds and mutual funds, according to data from research firm Morningstar Inc. This stratospheric growth has fueled concerns about greenwashing — when companies exaggerate their environmental benefits — and prompted criticism for having limited real-world impact on large problems such as climate change

and income inequality.

While institutional players are already highly attuned to ESG considerations and can often get the information they need about what's in a fund, retail investors are less able to dig into a portfolio's underlying assets and are "naturally more at risk of greenwashing," said Quinn Curtis, a professor at University of Virginia School of Law.

The proposals are the second set of major ESG-related policy changes that the agency is considering under Gensler. In March, the SEC announced plans to require companies to reveal detailed information about their greenhouse gas pollution and to outline the risks a warming planet poses to their operations.

Asset managers' ability to comply will depend on how much information they can get from the companies they invest in, said Sandra Peters, head of financial reporting policy at the CFA Institute.

The investment industry will spend the coming weeks pouring over the details. The SEC will take public comment for as long as 60 days, and may revise the proposal before holding a second vote to finalize the regulation.

Bloomberg Green

By Lydia Beyoud and Saijel Kishan

May 25, 2022

Fitch: ESG in Credit - Exposure to Social Impacts Report

Related Fitch Ratings Content: ESG in Credit – Exposure to Social Impacts Report

Fitch Ratings-London/Hong Kong-26 May 2022: Social issues are rising in prominence for investors and other stakeholders and as such the exposure issuers have on shifting consumer preferences or social pressures and resistance can manifest as a credit risk in certain situations, Fitch Ratings says in the latest of its 'ESG in Credit' series.

These shifts are captured as part of Fitch's ESG Relevance Scores (ESG.RS) under the Exposure to Social Impacts (SIM) general issues. This category captures credit issues arising from shifting consumer preferences driven by a desire to avoid harm or do good. These shifts are largely outside issuers' direct control and can be highly dynamic over time. They can affect demand for products and services, impair operations and alter market shares.

Mitigation of risks associated with elements under social impacts, such as strikes, boycotts and shifting consumer preferences, therefore rests heavily on the level of awareness on the part of the issuers of these underlying shifts, and actions to manage their operations to limit their exposure.

The pharmaceuticals, energy and natural resources and tobacco sectors have historically been at the forefront of either regulatory action to manage social impacts, or face various levels of social resistance. With the proliferation of social media, the technology sector is also becoming increasingly exposed to regulatory and consumer shifts in attitudes. Some non-bank financial institutions (NBFIs), as well as certain pools of RMBS transactions, have a higher concentration of higher ESG.RS that indicate medium and high impact from SIM.

The ESG in Credit series provides insights on the credit relevance and materiality of sector-specific ESG credit issues.

'ESG in Credit – Exposure to Social Impacts Report' is available at fitchratings.com or by clicking the link above, It focuses on the SIM general issue within Fitch's ESG.RS framework and scoring templates.

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The SEC's Proposed New Cybersecurity Disclosure Requirements for Public Companies: What Do They Mean for Municipal Issuers and Borrowers? - Orrick

- Governmental entities have increasingly experienced cybersecurity incidents impacting their operations and finances over the last few years, with some breaches costing upwards of $40 million.
- Many issuers and borrowers of municipal bonds are taking steps to defend themselves against such attacks, and may also need to determine how and when to disclose such efforts and any material cybersecurity incidents to the municipal market.
- While the SEC's recently proposed disclosure rules for public companies regarding cybersecurity incidents and related policies do not apply to municipal issuers and borrowers (unless the borrower is a public company) and are not final, they do provide helpful context and guidance for how the SEC may view cybersecurity disclosures in the municipal market.

In light of these considerations, issuers and borrowers in the municipal market should:

- Review the SEC's proposed cybersecurity disclosure rules and their implications for the municipal market, specifically around incident reporting and periodic disclosure of risk management, strategy, and governance.
- Focus on their own cyber defenses and mitigation strategies, since this has been a particular focus of rating agencies on public companies when assessing the strength of a particular credit.

A Growing Problem

In recent years, governmental entities have increasingly experienced cybersecurity incidents impacting their operations and finances. According to a white paper published by KnowBe4 in 2020, the median cost of a data breach for a state was $1.87 million, with some breaches costing upwards of $40 million. Many issuers and borrowers of municipal bonds ("issuers and borrowers") are taking steps to defend themselves against such attacks. They may wonder how and when to disclose such efforts and any material cybersecurity incidents to the municipal market.

The SEC has proposed new disclosure rules for public companies regarding cybersecurity incidents and related policies and procedures. Since the SEC does not have the power to adopt similar rules for issuers and borrowers (unless the borrower is a public company), the proposed rules **do not** apply to issuers and borrowers. They do, however, provide useful context and guidance for how the SEC may view cybersecurity disclosures in the municipal market, specifically around incident reporting and periodic disclosure of risk management, strategy, and governance.

Our governance and data privacy teams published an article summarizing the proposed rules as applied to public companies generally and proposing steps public companies could consider taking now. Our public finance and data privacy teams have prepared this supplement to that article, summarizing the key takeaways for issuers and borrowers. **We encourage you to read this supplement together with the underlying article.**

Applying the SEC's Proposed Rules to the Municipal Market

The SEC's proposed rules fall into two categories: (1) incident reporting; and (2) periodic disclosure of cybersecurity risk management, strategy, and governance. We will treat each category separately.

Incident Reporting

Public Company Rules: The SEC's proposed rules reveal its focus on timely disclosure of material cybersecurity incidents on a public company's Form 8-K by requiring that material cybersecurity incidents are reported within four business days from the materiality determination.

The SEC's proposed rules do not provide specific guidance for what constitutes a material cybersecurity incident. They do provide that the required timing of a public company's Form 8-K filing is tied to the company's determination that the incident is material rather than to its discovery of the underlying incident.

Additionally, the requirement applies to compromises of the company's "information system," which includes systems owned or used by the public company and may include third-party information resources such as cloud infrastructure and service providers.

Finally, the SEC's proposed rules require periodic updates reflecting material changes or additions to previously disclosed incidents. That would include information regarding remediation.

Application to the Municipal Market: In the municipal market context, the disclosure analogue for a public company's Form 8-K is an issuer or borrower's material event notice filed pursuant to its continuing disclosure undertakings and SEC Rule 15c2-12.

Rule 15c2-12 does not specifically require issuers and borrowers to disclose material cybersecurity incidents. Such entities may disclose incidents through voluntary event notices on the MSRB's Electronic Municipal Market Access ("EMMA") website.

In addition, when issuers and borrowers speak to the market through offering documents,[1] quarterly and/or annual continuing disclosure reports, or other communications, they may want to consider disclosing recent material cybersecurity incidents. Issuers and borrowers may also want to consider focusing on developing and/or improving internal reporting systems to facilitate the discovery of and determinations of materiality regarding internal and third-party cybersecurity incidents.

Issuers and borrowers may want to consider the following questions when developing and/or improving reporting systems relating to cybersecurity incidents:

- Do you have a current and tested incident response plan?
- Do you have cybersecurity policies and procedures in place that require employees to quickly escalate cybersecurity incidents to those empowered to make materiality and disclosure determinations?[2]
- Do you have a process in place to assess the range and magnitude of financial impacts of a cybersecurity incident, as they become available, and memorialize materiality determinations?
- Do your contracts with third parties that make up your "information system" provide for incident reporting and the cooperation necessary to make materiality and disclosure determinations regarding third-party cybersecurity incidents?
- Do you have a process in place to track updates regarding previously disclosed cybersecurity incidents and provide such updates to those empowered to make materiality and disclosure determinations?
- Have you discussed with bond or disclosure counsel the implications of any cybersecurity incidents and possible voluntary disclosures?

Periodic Disclosure of Risk Management, Strategy, and Governance

Public Company Rules: The SEC's proposed rules also reveal a focus on public companies' internal risk management, strategy, and governance. Specifically, the proposed rules include changes to Regulation S-K, and corresponding changes to Form 10-K and Form 10-Q to require additional disclosures.

The proposed rules would require a public company to periodically disclose information about the processes of its board of directors and key management relating to cybersecurity issues. Specifically, the SEC proposes disclosure relating to "whether or how the board or board committee considers cybersecurity risks as part of its business strategy, risk management, and financial oversight." The agency would also require disclosure of whether or not a company has a Chief Information Security Officer (including that person's background and reporting line). In addition, the SEC's proposed rules require a public company to periodically disclose whether any members of its board have expertise in cybersecurity, and to provide detail regarding the nature of that expertise. The SEC's proposed rules reveal its increasing desire to obtain detailed and specific disclosures regarding a public company's internal processes and expertise relating to cybersecurity.

Application to the Municipal Market: In the municipal market context, the disclosure analogue for a public company's Form 10-K and Form 10-Q is an issuer or borrower's annual report and quarterly report (if any), respectively, filed pursuant to its continuing disclosure undertakings. As with cybersecurity incident reporting, there is no specific requirement that issuers and borrowers include in annual or quarterly reports information regarding internal risk management, strategy, and governance. However, given the SEC's marked focus on cybersecurity-related disclosure (including the two SEC enforcement actions in 2021 relating to data privacy incidents referenced in footnotes 1 and 2), issuers and borrowers may want to evaluate the quality of their disclosures in this area whether through voluntary event filings, annual and/or quarterly continuing disclosure reports,

offering documents, or other communications to the market.

More broadly, issuers and borrowers should review and update their cybersecurity policies and disclosure procedures. They may also want to focus on developing disclosures relating to existing cybersecurity policies and procedures they can update and adapt for quarterly and annual reports and offering documents. Given the SEC's focus on the expertise of individual directors or employees, issuers and borrowers may also consider collecting information regarding cybersecurity expertise that members of their governing bodies and key staff members possess and consider whether an internal Chief Information Security Officer position exists or can be created. In undertaking such efforts, we recommend that issuers and borrowers consider the following questions:

- Do you have comprehensive information security policies
- Have you had any privacy or security incidents that involve confidential or personal data?
- How does your governing body evaluate cybersecurity risk and what role does cybersecurity risk play in its decision-making process?
- Do you have a Chief Information Security Officer, or other individual designated as responsible for information security?
- Which members of your governing body and staff, including the Chief Information Security Officer, if any, possess expertise relating to cybersecurity matters?
- Do you have cyber insurance, and if so, what does it cover and what are the retention and limits?
- Do you conduct periodic risk assessments, and if so, have any identified risks been remediated or added to a security roadmap?
- Have there been any third-party security assessments, and if so, have the identified issues been remediated or added to a security roadmap?

Additional Considerations for the Municipal Market

National Federation of Municipal Analysts

The National Federation of Municipal Analysts published a white paper in November 2020 calling for municipal bond issuers to "conduct a cybersecurity assessment to start the process of addressing cybersecurity risks as soon as possible" and recommending best practices for cybersecurity risk disclosures. Issuers and borrowers may want to review the paper to understand the views of municipal investors in this area.

Rating Agencies

While the SEC's proposed rules focus on enhancing and standardizing cybersecurity disclosure for public companies, rating agencies remain focused on public companies' cyber defenses and mitigation strategies when assessing the strength of a particular credit. A recent Moody's survey revealed that approximately 93% of organizations surveyed have a cybersecurity manager, and approximately 57% of North American organizations surveyed maintain cyber insurance.[3] To remain competitive, issuers and borrowers may want to consider implementing a cybersecurity manager, maintaining cyber insurance, and instituting cyber defenses and mitigation strategies to maintain their relative credit strength.

What's Next?

The SEC's proposed disclosure rules for public companies regarding cybersecurity incidents and related policies are not yet final. Orrick will continue to monitor the proposed rules and any related enforcement actions by the SEC, along with potential implications for issuers and borrowers in the municipal market.

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[1] In *In re Pearson plc* (2021), the SEC imposed a penalty of $1,000,000 against Pearson plc because its risk factor disclosure implied only that the company faced a hypothetical risk of a data privacy incident and failed to disclose that the company had in fact already experienced such a data breach.

[2] In *In re First American Financial Corporation* (2021), the SEC imposed a penalty of $487,616 against First American Financial Corporation because, despite an employee's discovery of a security vulnerability, the company's reporting system was insufficient to ensure that the fact of the vulnerability was communicated to senior executives responsible for disclosure.

[3] *See* Cyber risk survey of issuers finds growing investments, but gaps in preparedness, Moody's Investors Service (March 31, 2022).

by Joseph Santiesteban, Sean Yates

May 17, 2022

Orrick, Herrington & Sutcliffe LLP

Fitch: ESG Relevance Limited for Most US Public Finance Ratings

Fitch Ratings-New York-16 May 2022: A small portion, 7%, of US public finance ratings (USPF) are affected by environmental, social and governance (ESG) considerations, Fitch Ratings says. Fitch's ESG Relevance Scores (ESG.RS) communicate the extent to which ESG factors affect ratings but do not provide commentary on the ESG practices or qualities of issuers. ESG factors are manageable for most USPF issuers. Fitch's report Where ESG Matters for U.S. Public Finance reviews 12 case studies that illustrate how ESG issues can affect ratings and highlights current ESG focus areas, including issuer disclosure, the transition to a lower-carbon economy and cybersecurity.

Governance is the most important factor, on a singular basis, assessed to have a medium or high relevance for 3% of issuer ratings. This reflects the influence of governance structure and effectiveness, policy formation, and financial performance on credit quality.

Social factors have become more prominent with the assignment of ESG.RS in the community development and social lending (CDSL) sector, conveying the positive rating effect for certain credits of federal agencies' support of housing agencies and the negative effects of unsafe environmental conditions among some housing providers. Overall, social factors influence 2% of Fitch's USPF ratings.

Continue reading.

America's Political Right Has a New Enemy No. 1: ESG Investors

The popular investing strategy is drawing new partisan attacks ahead of the US midterm elections

Heading into the hotly contested midterm elections, the American political right has a new rallying cry: Down with ESG.

Conservatives have identified the popular investing strategy, which accounts for environmental, social and governance risks, as part of a broader narrative about left-wing overreach and " wokeness" run amok. Utah Treasurer Marlo Oaks calls it "corporate cancel culture." Behind the rhetoric lie policies designed to sap the momentum of one of Wall Street's most successful initiatives in recent years, now worth $35 trillion globally. If it works, it will firmly ensconce ESG in the culture wars, galvanize voters and weaken the resolve of big asset managers to act on climate change and other big, societal issues.

West Virginians are already all too familiar with ESG, according to state treasurer Riley Moore. He's preparing a list of banks that, he says, will lose the state's business unless they declare they aren't boycotting the coal industry and other fossil fuels. "Certainly 'woke capitalism' is something they are very familiar with," he said. "We're facing threats from that in my state, right now."

The attacks on ESG escalated last week when former Vice President Mike Pence made the strategy a key theme in an energy-policy speech in Houston. A potential candidate for the 2024 Republican presidential nomination, Pence said large investment firms are pushing a "radical ESG agenda" and took aim at BlackRock Inc., whose Chief Executive Officer Larry Fink is a champion of sustainable investing, and others who have pressed for progress on climate change.

Pence added to the growing public attacks on ESG. On Wednesday, Tesla Inc. founder and libertarian influencer Elon Musk told his 94 million Twitter followers that " ESG is a scam," building on a March tweet in which he labeled the practice "the Devil incarnate." Republican megadonor Peter Thiel called ESG a "hate factory for naming enemies" in a speech at a Bitcoin conference in April, and the Twitter bio of right-wing pundit Glenn Beck now reads, "Against ESG before it was cool."

With gas prices rising and energy a key factor in Russia's invasion of Ukraine, it's becoming easier for Republicans to tie ESG to pocketbook issues of their constituents. Just as Critical Race Theory grew from a catchall for parents unhappy or worried about what their children were learning in public schools to successful efforts to seize control of local school boards, ESG opponents see an opportunity to aim voters' fears of inflation at the finance industry's efforts to combat global warming and other social ills.

It's also a new front in a longstanding battle against further restrictions on fossil-fuel industries, which give generously to Republican party candidates, and more corporate accountability. At the state level, Republican governors and other officials are finding new ways to block major Wall Street firms from state business, including managing pension funds and bond issues, if they apply ESG principles to other parts of their portfolios.

Nationally, the broadsides against ESG bolster calls to abandon, or at least relax, environmental standards in favor of "energy independence." It's also a partisan issue at the US Securities and Exchange Commission, which is trying to require companies to report on their greenhouse gas emissions. In a virtual meeting on the plan in March, the agency's only Republican commissioner, Hester Peirce, turned off her camera in protest, saying that she was trying to reduce her carbon footprint.

Republicans are increasingly using banks and "woke" companies as cudgels for their base voters, said Reed Galen, a co-founder of the anti-Trump group, The Lincoln Project. "If you're taking on a company who has environmental and social justice goals, you don't have to explain ESG to the voters.

All you have to do is say ‘woke corporation.’”

In the past few years, as the world became more aware of the risks posed by global warming and social unrest, financial firms have rushed to offer investments that promise to account for those risks — and maybe even minimize them. With an ESG slant on everything from loans to complex derivatives, assets are set to balloon to $50 trillion worldwide by 2025, according to estimates from Bloomberg Intelligence.

In the US, a big proportion of that is via public pension funds, which are overseen by state or local officials, or in private sector retirement plans, and receive preferential tax treatment. In response to new federal rules that would allow pension funds to consider ESG alongside traditional fiduciary factors in making investing decisions, almost two dozen states registered their objection, saying the rules would allow investments to be guided by “social causes and corporate goals, even if it adversely affects the return to the employee.”

Those states are increasingly considering legislative action. State lawmakers and treasurers have for years been concerned that politically motivated investing strategies reduce long-term profits, said Jonathan Williams, chief economist at the American Legislative Exchange Council. The conservative group, which writes model legislation, is looking to prevent public pensions from making investments using ESG.

Credit ratings agency S&P Global Inc. also has come under fire for using ESG information to evaluate municipal debt. In West Virginia, Moore joined several state treasurers last month to demand the ratings agency drop ESG factors from its rating system. His state got a negative social score and a moderately negative environmental score, signaling higher risk than the vast majority of states, which are rated neutral.

“The ESG movement is nothing but a slippery slope,” Moore said, cautioning that states will be forced to “bend the knee to the woke capitalists or suffer financial harm.”

S&P Global declined to comment on specific states and instead referred to a paper it published May 9 explaining how its ESG credit indicators work.

Kentucky, Texas and West Virginia have passed legislation that requires financial firms to say whether they have policies that limit doing business with oil, gas and coal companies, a common practice for firms that have made pledges to reduce their own carbon footprint. Banks that demur could lose their licenses in those states. Another 12 states are considering similar measures.

“Once ESG becomes commingled with corporate wokeness, it can become a powerful way for anti-corporate right wingers to talk about it and galvanize voters,’’ said Chris Stirewalt, an expert in US politics, voting trends and public opinion at free-market think tank American Enterprise Institute.

In addition to shunning oil, gas and coal producers as part of climate change policies, investors and employees have encouraged companies in recent years to take positions on LGBTQ rights, gun control and other issues that add to rancor among Republican voters.

Most recently, companies have begun to address the third rail of political issues: abortion. In March, Citigroup Inc. made waves when it said it would cover the travel and medical costs for any of its employees who needed to cross state lines to seek an abortion or other reproductive health care. In response, a Texas lawmaker said the bank could face criminal charges under that state’s abortion law, and Republican members of Congress called for the cancellation of US government contracts with Citigroup, which provides the credit cards that members of the US House of Representatives

use to pay for flights, supplies and other goods.

Spokespeople for Citigroup and BlackRock declined to comment. A spokesman for Thiel didn't respond to messages, nor did representatives for Tesla, run by Musk.

Few expect the Republican attacks on ESG to vaporize the industry. As of now, roughly $3.4 trillion of public retirement money is invested in line with ESG strategies of some sort, according to the sustainable-investing industry group US SIF. Some of the bigger, more liberal states like California and New York are pushing for more restrictive ESG screens for state funds, not less. What's more, many of the world's biggest financial institutions have their own goals to cut emissions, which include reducing the amount of business they do with heavy polluters — whether they bill it as ESG or not. Many also have set targets for workforce diversity and elevating women in management, neither of which are politically popular among the right.

Still, the political pressure seems to be taking a toll. BlackRock sent a letter this week to the Texas state comptroller, rebutting the assertion that the firm boycotts the oil and gas industries, and Fink has made it clear he opposes divesting from fossil-fuel companies. The firm also said this year that it won't back as many shareholder efforts to push companies to reduce their emissions compared with 2021. JPMorgan Chase & Co. is also taking steps to re-establish itself in Texas's muni-bond market, about eight months after a new law forced that bank out of most deals because of its policies on guns and fossil fuels.

And if Wall Street's usual suspects can't be persuaded, others are eager to step in. With the backing of hedge fund manager Bill Ackman and Thiel, Vivek Ramaswamy, a pharmaceutical investor and author of "Woke Inc.," has started an investing firm that attempts to be an antidote to the "political agendas" and "stakeholder capitalism" of bigger money managers.

In Utah, state treasurer Oaks pointed to real pain points for his constituency. Dixie Power, for example, which delivers power to roughly 25,000 customers, recently learned its longtime auto insurer wouldn't renew coverage. The utility owns a coal-burning power plant and has stakes in two others, and the insurance company is phasing out business with companies that derive profits from coal, according to Colin Jack, the firm's chief operating officer. The co-op is also set to lose insurance coverage for its coal mine from Lloyd's of London for the same reason.

Fueled by frustration with that and what he sees as other government intrusion into the energy sector, Jack is running as a Republican for a seat in the Utah state legislature.

He may be in line for a powerful endorsement. On Wednesday, less than three hours after tweeting that ESG is a scam, Musk wrote that although he'd voted Democrat in the past, "I can no longer support them and will vote Republican."

Bloomberg

By Jeff Green and Saijel Kishan

May 20, 2022

— With assistance by Benjamin Bain, and Mark Niquette

Ducking the Culture Wars Isn't an Option for Companies Anymore. Fighting Back Is.

The culture wars are heating up for U.S. businesses. Many will duck. But those who want to stand their ground should look to Citigroup, the company that messed with Texas and lived to tell the tale.

In March 2018, after a gunman killed 17 people at Marjory Stoneman Douglas High School in Parkland, Fla., then Citigroup CEO Michael Corbat announced a new firearms policy for the bank. The policy, with some caveats, prohibits retailers that are customers of the bank from offering bump stocks or selling guns to people who haven't passed a background check or are younger than 21.

As reported by Bloomberg News, the national gun lobby went into overdrive, accused Citi of being " woke" and lobbied for a law passed last year by Texas Republicans that forbid the state from working with any companies that "discriminate" against the firearms industry.

At stake for Citi and other banks that adopted similar policies was $58 billion in debt underwriting fueled by population growth and infrastructure needs. Citi's ranking as the largest Texas munis manager plummeted while the bank hashed out a recognition from the state attorney general that the policy did not discriminate.

In December, Citi, without making any change to its gun policy, finally resumed business with the state of Texas. It is now leading underwriting for a $1.2 billion bond sale for the Dallas Fort Worth International Airport.

Citi quickly found itself fighting on another front in Texas. Corbat's successor, CEO Jane Fraser, in response to a Texas law banning abortions after six weeks of pregnancy, announced that Citi would pay travel expenses for employees needing to travel out of state to have access to adequate medical resources. "What we did here was follow our past practices. We respect everyone's view on this subject," Fraser said.

Texas state Rep. Briscoe Cain warned Citi that employees who travel outside Texas for an abortion could face criminal charges. He said he would introduce legislation to bar Citigroup from underwriting municipal bonds—again.

Citi has not issued any comments in response. But by standing up to Texas on guns Citi has set a precedent for ignoring the grandstanding and carrying on business as usual. For all the companies that want to demonstrate social purpose and care for employees' needs, but worry about alienating government stakeholders, breaking through the political noise to stand up for values isn't too hard.

In 2019, 181 CEOs of America's biggest companies signed on to a commitment by the Business Roundtable redefining the purpose of the corporation to serve all stakeholders, including workers, as well as shareholders.

The commitment covered rewarding hard work and helping workers adjust to the rapid pace of change in the economy. "We foster diversity and inclusion, dignity and respect," the statement says.

The statement was a reversal of economist Milton Friedman's popular view that shareholders are the only ones who count. It invited debate as to whether companies really should think about their stock price less and pay more attention to their employees. Perhaps without realizing it, the statement also placed them squarely in the middle of the so-called culture wars.

Advocates have pointed out that many of the signatories to the statement have fallen short in their

pledges to uphold the interests of all stakeholders. Companies have faced pressure to engage on voting rights, Black Lives Matter, abortion, LGTBQ issues, climate, and #MeToo. Covid-19 vaccination requirements also entered the debate.

This has set companies up to enter politics in a way they studiously avoided before, and not just in Texas. Republican governors in Florida and Georgia are now policing business, as the columnist Heather Cox Richardson puts it.

Disney's confrontation with Gov. Ron DeSantis over education legislation his opponents have labeled the "Don't Say Gay" law put CEO Bob Chapek to the test. He signed the Roundtable commitment. But he first tried to avoid getting involved, saying he didn't want the controversy to become a political football.

His workforce revolted and forced him to apologize to them and stand up to Gov. DeSantis.

Now Chapek is fighting Florida to retain tax breaks and governance of the special district created for Disney, the state's largest employer, since its inception.

The abortion fight has raised the stakes even higher.

The draft under consideration by the Supreme Court to overturn Roe v. Wade has turned the social purpose debate upside down. The landmark ruling in 1973 gave women the freedom to decide if they wanted an abortion. If the ruling takes away that right on a federal level, states like Texas, Georgia, Alabama, Arkansas and Florida have strong anti-abortion laws that will kick in. Other states that would also have the power to decide may follow.

For companies that offer healthcare plans that cover abortion and follow federal guidelines of offering equal healthcare to all their employees, this is a practical problem, as much as a moral one. Many operate in states were abortion would become illegal. Companies such as AT&T, which signed the Business Roundtable statement, may not believe it obligates them to take a stance on abortion. The company has stayed with a policy of public silence on the topic.

But nearly 200 CEOs have recognized that the right of women to make their own decision about abortion rights is good for business. It's an important part of Americans deserving a life of "meaning and dignity," as the Business Roundtable statement put it. Like Citi, Amazon, Starbucks and Tesla have all announced they would help their Texas employees travel for out-of-state abortion services.

For companies that don't live up to their social-purpose commitments, there's a good chance their employees will hold them accountable. Ducking is no longer an option. Citi's experience shows they can put their money where their mouth is and live another day.

Barron's

By Laurie Hays

May 20, 2022

'Woke Bond Rating'? The Muni Finance Fight Over ESG Scores.

Utah officials recently lashed out at a rating agency's use of environmental, social,

governance rankings. Investors have an appetite for the metrics, but critics say they're too subjective.

Welcome back to another edition of Route Fifty's Public Finance Update! I'm Liz Farmer and this week, I'm looking at the latest squabble over ESG evaluation—assessing governments' long-term environmental, social or governance risks. As always, send feedback and tips to: publicfinance@routefifty.com.

ESG evaluation has always been a somewhat contentious issue in the investment community because data on those metrics are not standardized. But a recent move by S&P Global to assess states' ESG exposure is sparking new debate, and has conservative lawmakers and interest groups fighting back in one of the most concerted efforts yet to discredit the practice.

At issue are new "ESG credit indicators" S&P released in late March. Each state was given a report card on its environmental, social and governance factors and assigned a ranking of 1 (positive) to 5 (very negative) on each factor. States all generally scored twos and threes for each category. "ESG credit indicators," said S&P in a recent FAQ, "provide additional transparency on what's already incorporated into our credit rating analysis."

Continue reading.

Route Fifty

By Liz Farmer

MAY 17, 2022

SEC's Sanchez Offers Guidance on ESG.

Issuer fears that ESG regulation will lead to disclosure trouble are overblown, the Securities and Exchange Commission's muni office chief said Wednesday.

Dave Sanchez's comments were part of the National Federation of Municipal Analysts' 2022 Annual Conference, where panelists spent considerable time discussing the recent ESG initiatives underway at the SEC and Municipal Securities Rulemaking Board.

Sanchez addressed industry concerns that any disclosure regime centered around ESG will be an exercise in over-disclosure.

The SEC's 2020 guidance on voluntary disclosures related to COVID-19 has received mostly positive marks from the market, but the Commission may be considering expanding some of the provisions on cautionary language going forward.

"We lean heavily on the 2020 SEC statement from the chair and the director of the Office of Municipal Securities talking about cautionary language about your disclosure," said Emily Brock, director of the federal liaison center at the Government Finance Officers Association. "Always very glad to hear Dave mention that there is thinking at the SEC about maybe expanding that information beyond COVID-19 disclosures."

Panelists also used their time to work through how regulators, investors and issuers handle

materiality.

“As a practitioner, I kind of always thought of it as like you’re trying to cross a river from the information you’re holding to disclosing it and there’s really one rock in the middle and that’s materiality,” Sanchez said. “Part of the job of the SEC really is to provide additional touch points in different contexts that help people get across the river to actually disclose this information.”

Panelists agreed that some issuers feel they have the right to define materiality on their terms, which is not the standard as defined by the SEC.

“As a former issuer myself, I actually think I suffered from a misunderstanding of securities law as I thought I got to define materiality,” said Mark Kim, chief executive at the MSRB. “It’s the investors decision to make.”

The Supreme Court has ruled that information is material if it would matter in the investment decision of a reasonable investor.

“It’s not really in the eye of the beholder,” Sanchez said. “There is a standard, it has to be reasonable investors, it’s not any investor.”

But Sanchez ultimately believes that ongoing dialogue with underwriters, bond counsel or others around materiality, and if it’s well-documented, will provide some protection from the SEC.

“If you have a good-faith discussion about whether something is material or not, that ends up providing a lot of protection under securities laws,” Sanchez said.

The MSRB’s controversial request for information on ESG also served as an important pillar for the discussion. Kim expressed that he was surprised by comments that questioned why the MSRB was asking these sorts of questions, when he thought market participants would be asking why the board didn’t do this sooner.

Kim compared the ESG RFI to the RFI issued in 2018 on third-party yield curves, which is still a concern that persists today.

“While I’ll be the first to admit that we have absolutely no regulatory authority over third-party vendors that are offering yield curves and benchmarks to the industry, we do have the responsibility to ask that question,” Kim said.

SOURCE MEDIA

By Connor Hussey

May 18, 2022

A Muni Minute: Tit-for-Tat

Municipal investors often sift through various issues that include underfunded pensions, a lack of market liquidity, and inconsistent financial disclosure. However, there is a new area of concern that is causing indigestion among market participants: political and corporate agendas.

On April 22, Florida Governor Ron DeSantis signed a bill dissolving a handful of special taxing

districts created prior to 1968, most notably the Reedy Creek Improvement District (Reedy Creek). The move was significant since Reedy Creek allows The Walt Disney Company to exert considerable governmental autonomy over the area within and around its nearly 25,000-acre theme park. Interestingly enough, the legislation was introduced not to provide any sort of societal or economic benefit, but to penalize Disney for denouncing a controversial gender bill that was signed into law earlier this year.

While the ability of the special district legislation to withstand legal challenges remains uncertain, questions still remain regarding the treatment of nearly $1 billion of municipal bonds issued by Reedy Creek. State law dictates that outstanding bonds from a dissolved special district will be transferred to overlapping municipalities, which in this case largely includes Orange County, FL. However, whether the county chooses to honor the bonds is unclear, potentially creating a larger issue for the state and more importantly, for investors.

More troubling is that this is not the first instance in which politics have collided with the municipal market. In 2018, multiple large financial institutions began implementing policies that restricted business relationships with certain firearms manufacturers. In response, Texas Governor Greg Abbott, along with the governors of several other states that derive a material amount of economic activity from the firearms industry, signed laws that prohibited municipalities from having contractual relationships with companies that discriminate against the firearms industry. The Texas bill effectively prevented Citi Group, the largest municipal underwriter in the state, from doing business with local municipalities. Both actions caused concern in the capital markets, with the former showing the power that major financial institutions can wield to effectively cut off financing to certain sectors of the market, and the latter effectively reducing competition amongst municipal underwriters, possibly resulting in increased borrowing costs for public finance issuers.

Legislation and corporate actions fueled by political agendas that unnecessarily rile the capital markets represent a policy mistake, in our opinion, especially when the measures effectively restrict consumer choice. Investors can abstain from investing in securities that do not meet their investment criteria, and issuers have the ability to work with whichever financial institution that they believe will help them best accomplish their objectives. However, corporate policies and legislation that instead make these choices for the end user generally do more harm than good in that they tend to limit competition, push higher costs onto consumers, and are typically met with retaliatory measures.

While it is nearly impossible to predict the next target of a political attack, investors should be wary of municipalities with an overreliance on any one specific industry or company, potentially leaving them in the crosshairs of political battle between corporate America and state legislatures. We do not foresee any related issues with municipal sectors that rely on state appropriations for a significant portion of their funding, including K-12 schools and public higher education institutions. This is because education-related funding cuts are typically politically unpalatable, and generally are only utilized in the event of a state budget shortfall. Nevertheless, we view these politically charged disruptions as one-off events, and municipal bonds remain an excellent option for investors looking for tax-exempt income with very limited credit risk.

SAGE ADVISORY

By Brett Adelglass, Sage Portfolio Management

MAY 10, 2022

How to Avoid Political Jockeying With ESG Bond ETFs.

374Like so many current issues, environmental, social, and governance (ESG), at least in the eyes of some experts, has an element of political polarization to it.

That situation is amplified by lack of clarity and uniformity pertaining to how index providers score securities on the basis of ESG, prompting some experts to speculate that this could be a legitimate issue to contend with as the universe of fixed income assets aiming for ESG consideration grows.

As reflected by exchange traded funds like the newly minted SPDR Nuveen Municipal Bond ESG ETF (MBNE), there is demand for fixed income strategies that combine bonds and ESG principles. In fact, despite its rookie status, MBNE could be at the right place at the right time because issuance of green munis is soaring, while some state financial regulators are clamoring for more clarity on exactly what constitutes ESG.

For example, Utah recently clashed with index giant and credit ratings agency Standard & Poor's (S&P) over ESG ratings, asserting that the firm's standards are too ideological.

"In addition to rating governments on meaningful financial criteria, in March the biggest of the top three credit-rating firms began to apply an environmental, social and governance, or ESG, rating system. But Utah isn't about to submit to these subjective standards. State officials, including myself, recently wrote a letter to S&P objecting to the ESG indicators and ratings it has assigned to Utah and calling for the company to withdraw them," writes Utah Treasurer Marlo Oaks in an op-ed for the Wall Street Journal.

Regarding MBNE, the ETF can allay concerns on both sides of the aisle. For starters, Utah isn't one of the top 10 state exposures in the new ETF, and that group combines for about 70% of the fund's roster.

Second, MBNE is actively managed, indicating that it can skirt some of the thorny political issues associated with some parts of ESG investing while focusing on the business of identifying the best opportunities among green municipal bonds.

That's not to say MBNE doesn't have standards — it does. Bonds entering the fund must meet certain ESG traits. However, as an actively managed fund, MBNE has flexibility in a space that needs it.

Markets "encapsulate many different views of the future and their organic structure allows for quick adaptation. ESG scores, by contrast, rigidly hold to one viewpoint and are slow to pick up on changes in the world," adds Oaks.

ETF TRENDS

by TOM LYDON

MAY 12, 2022

Fitch: Where ESG Matters for U.S. Public Finance

View the Fitch Special Report.

Mon 16 May, 2022

MSRB Analysis Finds Notable Shift in Trading Volumes in Municipal Market Over Last 15 Years.

Washington, D.C. — A new MSRB analysis reveals a significant decrease in trading volumes in the municipal securities market over the 15 years from 2007 through 2021, mainly due to a dramatic decline in the variable rate market. The report also identified spikes in trading volumes and unique trading activity during periods of market disruption or dislocation.

Over the 15-year period studied, the market saw a 67% decline in par amount traded and a 16% decrease in the number of trades, with the declining trend in number of trades most apparent in recent years. While yields also have declined significantly over the last 15 years, during periods of market disruption or dislocation, such as the global financial crisis and the start of the COVID-19 pandemic, trading volumes and yields generally tended to spike amid a notable rise in customer sales—both in terms of par traded and number of trades—and decline in customer purchases as compared to other trade types.

“Of all the periods of market disruption during the last 15 years, the global financial crisis of 2008 had the most lasting impact on the municipal securities market,” said John Bagley, chief market structure officer. “In particular, the sudden and dramatic decline in trading of variable-rate municipal securities in 2008 led to a fundamental shift in the municipal market structure over the subsequent years.”

The number of trades of variable-rate securities fell from 25% of the overall market in 2007 to an average of just 4% by 2009, while par traded fell from 70% of the overall market in 2007 to 44% in 2009, following a significant decrease in trading associated with tender option bond programs and the auction rate securities market. The variable-rate market has never recovered, with the number of trades averaging between 1% and 4% of overall trades between 2009 and 2021 and par amount traded declining further to 23% of total par traded in 2021.

Meanwhile, trading in the fixed-rate municipal market has not seen the same level of change as the variable-rate market. While trade sizes have increased, particularly in the tax-exempt market, the overall number of trades and par amount traded in the fixed-rate market remained relatively steady for the 10 years between 2007 through 2017, though they declined significantly starting in 2018, with 2021 volumes reaching the lowest levels in terms of number of trades and the second lowest in terms of par amount traded since 2007.

Date: May 11, 2022

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S&P Hits U.S. States With Politicized Credit Scores: WSJ Opinion

The ratings agency seeks to penalize fossil-fuel producers. Its 'ESG' push is unlikely to end there.

Ideological criteria will now influence the credit ratings of state and local governments, thanks to S&P Global Ratings. In addition to rating governments on meaningful financial criteria, in March the biggest of the top three credit-rating firms began to apply an environmental, social and governance, or ESG, rating system. But Utah isn't about to submit to these subjective standards. State officials, including myself, recently wrote a letter to S&P objecting to the ESG indicators and ratings it has assigned to Utah and calling for the company to withdraw them.

ESG is sometimes dressed up to look objective with quantitative "metrics" and complex "analytical frameworks." But this blurs the distinction between subjective judgments and objective financial assessments.

S&P Global says it "incorporates [ESG] risks and opportunities into the credit rating analysis" of public issuers. This includes ambiguous and open-ended categories such as how a state scores on "managing carbon," "political unrest stemming from community and social issues" and "adverse publicity that results in reputation risk." Leaving no doubt as to the measurement's subjectivity, S&P notes, "reflecting ESG risks and opportunities within our credit rating analysis will require a qualitative view of an entity's capacity to anticipate and plan for a variety of emerging risks." Unlike quantifiable financial metrics, this qualitative view depends entirely on the beliefs of whoever constructs it.

It's easy to see that those beliefs are left-wing. S&P assigns a lower ESG score to states that have both "physical risks" like earthquakes and natural disasters and a larger percentage of their economy tied to natural resource extraction, such as Texas, Alaska and Louisiana. S&P's Environmental category, after noting federal-state partnerships' financial mitigation of natural disasters, focuses its assessment on the costs of making the transition to "net zero" and the policy changes it predicts will be necessary to "curtail" greenhouse-gas emissions.

Certainly, if a state's finances are overly concentrated on any one particular industry this will affect its financial outlook because of the risk that revenue could decline should that industry's fortunes contract. But a traditional credit rating takes into account the diversity of industry in a state already, so why create an ESG metric that could be politicized? Instead of focusing on the financial risk associated with economic concentration, the ESG metric highlights if a state or local government allows what S&P thinks is too much oil, gas or coal extraction.

Further, there are national security, economic and even environmental benefits for U.S. states to produce traditional energy. Many countries are searching for sources of natural gas and oil so they can lower their dependence on Russia after its invasion of Ukraine. In that environment, states like Texas, Alaska and Louisiana have a tremendous market advantage and could see improved cash flows. Not only are their fossil fuel revenues benefiting a free democracy, Russia's natural gas exports to Europe burn 41% dirtier than American natural gas. Exporting U.S. natural gas would create a significant environmental benefit. Authoritarian regimes like Russia threaten, among other things, the environment, human rights, free societies and democratic government—all factors that should be important to ESG proponents. That S&P's ESG metrics completely ignored or missed these variables exposes some of the major flaws of ESG ratings. Such scores place a value judgment on political issues that do not have one right or wrong answer, are highly complex, and are impossible to predict.

As the Russian situation has shown, ESG assessments depend on variables that can change rapidly. Before Russia attacked Ukraine, Europe was moving away from fossil fuels and military spending. That changed almost overnight. This is why markets are so valuable; they encapsulate many different views of the future and their organic structure allows for quick adaptation. ESG scores, by contrast, rigidly hold to one viewpoint and are slow to pick up on changes in the world. The minds behind S&P's ESG metrics seem to believe that a transition to green energy is inevitable and therefore punish states that produce traditional energy for "climate transition risk." But no one really knows what this "climate transition" will look like. There are no widely accepted, economically viable alternatives to fossil fuels in the market. No one knows where they'll come from, what they'll be or when they'll arrive.

ESG metrics' false certainty about future events, and consequent inability to keep up with unanticipated current events, causes capital to be misallocated. They create bubbles in favored industries while starving others that could be profitable.

The solutions to our most difficult challenges—such as climate change—can come only through innovation. Foisting rigid ESG factors onto the market discourages innovation by mandating conformity, penalizing creativity and punishing the industry with the greatest incentive to find alternatives—the energy sector. Fracking has reduced U.S. carbon emissions immensely, but it could cost you under S&P's ESG metrics.

Utah has prudently managed its finances over decades and as a result maintains the highest possible credit rating from all major firms, allowing the state to borrow money at the lowest rates and save taxpayer dollars. But under the new ESG regime, those financial factors may be supplanted by subjective, political ones.

These metrics also threaten Utah and other states' democratic sovereignty. The ESG disclosures many corporations have felt compelled to release have also led to frivolous legal action and shareholder resolutions, an additional fiscal drag on businesses. Extending this regime into the municipal sphere is an invitation to litigation and other coercive tactics that will sabotage states' self-determination and independence.

States like Utah value our constitutional republic, which has ensured freedom, and free markets, which have fostered innovation and generated prosperity for generations. Any states, governmental jurisdictions, corporations, individuals, and investors who also hold those beliefs should join us in standing against ESG.

The Wall Street Journal

By Marlo Oaks

May 8, 2022 5:22 pm ET

Mr. Oaks is treasurer of Utah.

State Blue Sky Laws: Shedding Light on Exclusions from Municipal Bond Exemptions

We continue our series exploring the lack of uniformity – and sometimes lack of guidance – that makes it challenging to interpret state Blue Sky laws. Today's example addresses the exclusion from

the use of the municipal issuer exemption if the securities being issued are paid from a non-governmental source.

Summary:

Some states exclude from the municipal exemption the registration of municipal securities that are paid from a non-governmental industrial or commercial enterprise, unless the payments and insured are guaranteed by a person whose securities are exempt from registration under certain other enumerated sections of the law.

Issue:

There is substantial disagreement among these states as to whether conduit 501(c)(3) bonds, student loan bonds and single family mortgage revenue bonds constitute bonds payable from revenues to be received from a non-governmental industrial or commercial enterprise.

Sub-Issue:

What is a non-governmental industrial or commercial enterprise? Most states do not include a formal definition, leaving practitioners having to interpret those state's laws with little or no guidance. One state that does define non-governmental industrial or commercial enterprise includes non-profit corporations in the definition, but another state excludes non-profit corporations within the definition of what is a non-governmental industrial or commercial enterprise. This is confusing to say the least – making one struggle to reconcile these polar opposite approaches.

Bottom line:

State opinions can sharply differ regarding exclusions from municipal bond exemptions. The lack of guidance and uniformity can make practicing in this area confusing, which is why it's key to rely on experienced consultants.

by Christopher Andreucci

May 12, 2022

Harris Beach PLLC

GASB Issues Omnibus Statement Addressing Wide Range of Practice Issues.

Norwalk, CT, May 9, 2022 — The Governmental Accounting Standards Board (GASB) today issued guidance addressing various accounting and financial reporting issues identified during the implementation and application of certain GASB pronouncements or during the due process on other pronouncements.

The issues covered by GASB Statement No. 99, *Omnibus 2022*, include:

- Accounting and financial reporting for exchange or exchange-like financial guarantees
- Certain derivative instruments that are neither hedging derivative instruments nor investment derivative instruments
- Clarification of certain provisions of:
  - Statement No. 34, *Basic Financial Statements—and Management's Discussion and Analysis—for*

State and Local Governments
  – Statement No. 87, *Leases*
  – Statement No. 94, *Public-Private and Public-Public Partnership and Availability Payment Arrangements*
  – Statement No. 96, *Subscription-Based Information Technology Arrangements*
- Replacing the original deadline for using the London Interbank Offered Rate (LIBOR) as a benchmark interest rate for hedges of interest rate risk of taxable debt, with a deadline of when LIBOR ceases to be determined by the ICE Benchmark Administration using the methodology in place as of December 31, 2021
- Accounting for the distribution of benefits as part of the Supplemental Nutrition Assistance Program (SNAP)
- Disclosures related to nonmonetary transactions
- Pledges of future revenues when resources are not received by the pledging government
- Updating certain terminology for consistency with existing authoritative standards.

The requirements of Statement 99 that relate to the extension of the use of LIBOR, accounting for SNAP distributions, disclosures for nonmonetary transactions, pledges of future revenues by pledging governments, clarifications of certain provisions in Statement 34, and terminology updates are effective upon issuance. The requirements related to leases, PPPs, and SBITAs are effective for fiscal years beginning after June 15, 2022, and all reporting periods thereafter. The requirements related to financial guarantees and the other requirements related to derivative instruments are effective for fiscal years beginning after June 15, 2023, and all reporting periods thereafter. Earlier application is encouraged and is permitted by individual topic to the extent that all requirements associated with an individual topic are implemented simultaneously.

Muni Audit Reporting Times Worsened Over Last Decade.

Municipal bond issuers took an average of 164 days from the close of their fiscal years to complete their comprehensive annual audits in 2020, up from 147 in 2009, a worsening trend that is beginning to affect issuers' credit ratings.

That's according to Merritt Research Service and the University of Illinois Chicago's Government Finance Research Center's new report comparing municipal bond issuers' audit times.

"In the interest of good governance and transparency and having adequate information to properly price these issues in the market, we felt that this is really important in terms of bringing attention to this issue," said Deborah Carroll, director of the Government Finance Research Center at the University of Illinois Chicago. "Unfortunately, the trend is going the wrong way."

Corporate bond issuers have median audit times of 60-90 days due to Securities and Exchange Commission requirements. Municipal bond issuers report audit times which are two to three times longer, averaging 140 to 160 days.

Late audits do weigh on ratings. S&P Global Ratings put New Orleans and 12 other local governments on a negative watch last week over failed filings.

"The withdrawal of the affected ratings could follow if we do not receive fiscal 2020 financial statements within 30 days," the agency said. "We consider the financial statements necessary to maintain and assess our ratings on these issuers. Accordingly, the ratings are now at risk of being

withdrawn, preceded by any change to the rating we consider appropriate given available information."

If issuers provide their 2020 financial statements within 30 days, S&P said it would conduct a full review and take a rating action within 90 days of the negative watch action.

Both co-authors of the report stressed the timeliness of the report considering such recent actions by S&P.

"We think that's an appropriate action by the rating agencies and it's really needed from the marketplace itself in order to recognize that there's greater risk where there's not timely disclosure," said Rich Ciccarone, president of Merritt Research Services.

The report divides muni bond issuance into categories of revenue bonds, which includes hospitals and healthcare systems, community colleges, private higher education, public higher education, airports, retail electric, toll roads, water and sewer and wholesale electric. The report also includes government bonds, which are split up by cities, counties, dedicated tax, school districts and states and territories. All categories' audit times have increased in the period from 2009-2020.

The report cites community colleges as having the largest increase in median audit time, 24 days, but notes a potential cause in the significant growth in the number of issuers between 2009 and 2020, which increases the variation in audit completion times among individual issuers.

Issuers in the hospital and healthcare sector increased their median audit time by 10 days, water and sewer issuers by 9 days, and retail electric sector issuers increased by 8 days. Public higher education fared better, increasing a median of 1 day and toll road issuers increased by just 2 days in the period 2009-2020.

For what is designated governmental bond sectors, school districts increased their audit time by 22 days, counties increased by 16 days, the dedicated tax sector 11 days, cities by 10 days and states and territories worsened their audit time by 2 days.

But some audit times were affected significantly during the 2019-2020 period as a result of COVID-19, especially in the revenue bond category of health and higher education sectors.

"During this time, when staffs were short and people were becoming accustomed to remote work, we certainly expected audit times for all sectors to become slower," the report said.

But that isn't exactly how it turned out. Community colleges continued their lag in 2019-2020, worsening their median audit time by 13 days but issuers in public higher education increased their audit times by 5 days, followed by issuers of hospitals and healthcare systems which increased their reporting time by 4 days.

For government issuers during 2019-2020, issuers in the retail and wholesale electric and toll roads sectors maintain audit times that are considerably faster than all other sectors combined.

But states and territories are among the most affected by COVID-19, as the median audit time increased by 11 days between 2019 and 2020. The audit time for cities only increased by 2 days in the same time frame.

"Between 2019 and 2020 in most of the sectors, we do see an increase in audit times, as we would expect, because COVID-19 sort of screwed everything up for this time period," Carroll said. "But we're not seeing a huge increase in the timeliness of these audit completions."

But not all issuers wait years to complete their audits. The report also ranks the top 3 issuers in each category, as Port Authority of New York & New Jersey comes in first for airports, Sioux Falls, South Dakota comes in first for cities and Santa Barbara County, California wins for counties, all completing their audits in under 90 days.

“Generally speaking, that puts them very much on par with the private sector corporate bond issuers, which I think is a really great sign,” Carroll said.

By Connor Hussey

BY SOURCEMEDIA | MUNICIPAL | 05/03/22 02:12 PM EDT

Which Municipal Bond Issuers Have the Speediest Audit Times?

Compared with corporate bond issuers, municipal bond issuers typically take two to three times longer — 140 to 160 days — to complete their audits between fiscal year-end and the date of the Independent Auditor’s Report signature, according to data research from Merritt Research Services.

This year the Government Finance Research Center at the University of Illinois Chicago partnered with Merritt, which has been tracking and reporting the time it takes for municipal bond-related audits to be completed and signed after fiscal year-end since 2007, to develop its latest analysis.

The new report includes an overview of audit time trends since 2009 and identifies the timeliest audits for the 2020 fiscal year, grouped by municipal credit sector. The analysis covers the nearly 10,000 municipal bond audits in the Merritt database found in CreditScope.

Median audit times for municipal bond issuers have generally been increasing since 2009, especially between 2019 and 2020, most likely due to the onset of the COVID-19 pandemic.

Among the revenue bond sectors, wholesale electric, hospitals and health care systems, and private higher education had the fastest audit times for FY2020. For the governmental bond sectors, school districts and dedicated tax had the fastest audit times in FY2020.

Revenue bond sector issuers are generally faster in completing their audits than issuers in the governmental bond sectors, the analysis found.

Among the top performers in FY2020, all issuers except for states and territories completed their audits in 90 days or less, putting them on par with corporate bond issuers.

Interest groups ranging from bond investors to government watchdogs to regulators have regularly called for faster audit times from municipal bond issuers, said Deborah Carroll, director of the Government Finance Research Center at UIC.

“Timely audit reporting is essential for credit evaluation and proper pricing in the municipal bond market and is an important indicator of good governance and stewardship,” said Carroll, UIC associate professor of public administration.

While there are several newcomers highlighted in this year’s report, many of the top performers in FY2020 were also recognized in FY2019 suggesting consistent leadership in debt management, according to Richard A. Ciccarone, president of Merritt Research Services, an Investortools

Company.

“All of the 2020 audit time exemplars and audit firms deserve commendation, particularly those that remained among the fastest to complete their audits from last year,” Ciccarone said.

University of Illinois Chicago

3-May-2022

Seventh Circuit Provides Rare Guidance On “Statutory Liens” - Cadwalader

On April 21, 2022, the U.S. Circuit Court of Appeals for the Seventh Circuit issued a decision interpreting the Bankruptcy Code’s definitions of “statutory lien” and “judicial lien,” holding that a lien imposed by the Chicago Municipal Code was “judicial” rather than “statutory” because it arose partly as the result of a “quasi-judicial” process rather than “solely by force of a statute.” *In the Matter of Mance*, No. 21-1355, 2022 WL 1182416 (7th Cir. April 21, 2022). In the Seventh Circuit’s view, the fact that a “quasi-judicial” process functioned as an “essential prerequisite” to the imposition of the lien and determined the amount of the lien was sufficient for it to qualify as a “judicial” rather than a “statutory lien,” notwithstanding that the lien was ultimately imposed automatically by operation of a municipal ordinance rather than directly by a court order.

Statutory liens are an important tool in municipal finance, because unlike some other types of liens, they are not cut off by Section 552 of the Bankruptcy Code in the event of a municipal issuer’s bankruptcy.1 Whether a municipal investor will qualify as a “secured” or “unsecured” creditor in a municipal bankruptcy therefore may depend on whether that investor’s lien qualifies as a “statutory lien.” Notwithstanding the importance of “statutory liens” to municipal finance, however, judicial decisions on the nature of “statutory liens” are relatively rare, particularly at the federal appellate court level. The Seventh Circuit’s *Mance* decision now adds to the relatively small library of appellate court decisions that can offer issuers and investors guidance on the nature of “statutory liens.”

Background

The *Mance* appeal arose out of a long-running series of cases—including the U.S. Supreme Court’s 2021 decision in *Chicago v. Fulton*2 —in which the City of Chicago (the “City”) impounded motor vehicles for various parking- and driving-related infractions. The Chicago Municipal Code provides that any vehicles so impounded “shall be subject to a possessory lien in favor of the City in the amount required to obtain release of the vehicle.” M.C.C. § 9-92-080(f). The issue in this particular appeal was whether the City’s possessory lien on a vehicle that it had impounded should be deemed a “judicial lien” or a “statutory lien” under the Bankruptcy Code. If the lien was found to be “judicial” rather than “statutory,” then it would be avoidable pursuant to a provision of the Bankruptcy Code authorizing individual debtors to avoid liens on motor vehicles. See 11 U.S.C. §§ 522(f), (d)(2).

Definitions and Examples of “Statutory” and “Judicial” Liens

The Seventh Circuit concluded that the lien under the Chicago Municipal Code was “judicial,” not “statutory.” In doing so, it applied the Bankruptcy Code’s definitions of “judicial lien” and “statutory lien.”

Specifically, the Bankruptcy Code defines a “judicial lien” as one “obtained by judgment, levy,

sequestration, or other legal or equitable process or proceeding." 11 U.S.C. § 101(36). By contrast, a "statutory lien" is defined as a lien "arising solely by force of a statute on specified circumstances or conditions . . . , but does not include security interest or judicial lien, whether or not such interest or lien is provided by or is dependent on a statute and whether or not such interest or lien is made fully effective by statute." 11 U.S.C. § 101(53). The Seventh Circuit noted that, under these definitions, the classification of a lien depends on the events that must occur before the lien attaches, with a "statutory lien" arising "solely by force of a statute," and a "judicial lien" resulting from some type of "legal or equitable process or proceeding."

As an example of a "statutory lien," the Seventh Circuit cited a mechanics' lien, which by statute attaches to improved property once payment for a mechanic's work on the property is due and goes unpaid. Such a mechanics' lien may require a filing with a county clerk in order to be perfected, but this filing requirement, in the Seventh Circuit's view, did not constitute the type of "legal or equitable process or proceeding" that would convert the lien from a "statutory" to a "judicial lien."

By contrast, the "textbook" example of a "judicial lien," in the Seventh Circuit's view, was a court-ordered money judgment, where a court must enter judgment for the winning creditor before the lien can arise.

"Quasi-Judicial" Proceedings Give Rise to a Judicial Lien

With these definitions and examples in mind, the Seventh Circuit next turned to the specific procedures required in order for the City to obtain a lien on an impounded vehicle. The Court acknowledged that these procedures fell "somewhere in between" the easy examples of a mechanics' lien and a money judgment, but ultimately determined that the "quasi-judicial" nature of the required procedures placed the impoundment lien on the "judicial" rather than the "statutory" side of the line.

Among other things, before an impoundment lien can be imposed, the Chicago Municipal Code requires the underlying traffic violations to undergo an administrative process through which they become "final determinations of liability." As part of this administrative process, the vehicle owner can contest the charged violation in an in-person proceeding or by writing. If the vehicle owner is unsuccessful in this first phase of the process, the vehicle owner can also file an appeal under the Illinois Administrative Review Law. Only after the owner has lost the appeal does the traffic violation become a "final determination."

Following a "final determination," more legal process is required in order for the City to impound the vehicle if the fines go unpaid. The City must issue a notice to the vehicle owner, and the owner has the right to petition for a hearing to prove that she is not liable for the fines. Only after the owner failed to prevail at such a hearing would the City be able to impound the vehicle, at which point the impoundment lien would attach.

Notably, the Seventh Circuit acknowledged that the last step of lien attachment was "automatic," with the lien attaching automatically by operation of the ordinance upon impoundment of the vehicle, "without further action by a judge or quasi-judicial official." The City therefore had some basis to argue that the impoundment lien was a "statutory lien." The Seventh Circuit concluded, however, that it could not simply "ignore all the prior legal process that must occur before the City's possessory lien arises." In light of this prior legal process, the Court concluded that the impoundment lien did not arise "solely by statute," and instead was dependent on a "legal . . . process or proceeding." Therefore, the lien was a "judicial" rather than a "statutory lien."

Distinguishing the Third Circuit's *Schick* Case

In response to an argument by the City that the position ultimately adopted by the Seventh Circuit would create a circuit split, the Seventh Circuit attempted to distinguish the Third Circuit's decision in *In re Schick*, 418 F.3d 321 (3d Cir. 2005). The *Schick* case had some superficial similarities to *Mance*, because it addressed a New Jersey statute that imposed a lien on a motorist's property in the event the motorist failed to pay certain surcharges related to underlying traffic violations, including for reaching a certain number of violation points.

The Seventh Circuit nonetheless identified what it viewed as a "critical difference" between the processes leading to the liens in *Schick* and in *Mance*. Specifically, the New Jersey statute in *Schick* pertained only to surcharges, not to the underlying vehicle violations that were subject to judicial proceedings. The Third Circuit therefore concluded that "the underlying traffic proceeding charging the driver with a motor vehicle offense [was] too remote to constitute the required judicial process or proceeding necessary to find a judicial lien." On that basis, the Third Circuit concluded that the resulting lien was a "statutory lien."

In *Mance*, by contrast, the Seventh Circuit concluded that the statutory structure did not separate the underlying vehicle violation that was subject to quasi-judicial proceedings from any related fees (analogous to the "surcharges" at issue in *Schick*). Indeed, in *Mance* the amount of the lien itself was determined in the underlying quasi-judicial proceedings, and this lien amount included additional fees and penalties incurred in the course of those proceedings, whereas in *Schick* the amount of the surcharges was dictated separately by "statute and administrative regulations" and not determined by the underlying proceeding against the driver. The Seventh Circuit therefore concluded that in *Mance*, unlike in *Schick*, the quasi-judicial proceedings were "essential prerequisites for a valid impoundment lien," and were "not too far removed from the impoundment lien" for it to qualify as a "judicial lien."

The Seventh Circuit's method of distinguishing *Schick* suggests that, in determining whether a particular lien is "statutory" or "judicial," it may not be sufficient to perform a binary analysis of whether or not judicial proceedings play a role in the creation of the lien. Instead, it is necessary to analyze the precise relationship between any judicial proceedings and the creation of the lien, including how far "removed" the judicial proceedings are from the ultimate creation of the lien.

It will be interesting to see whether the City accepts the Seventh Circuit's attempt to distinguish *Mance* from *Schick*, or instead seeks review by the U.S. Supreme Court on the theory that *Mance* has created a circuit split between the Seventh and Third Circuits.

Tax Liens as Statutory Liens

In response to another argument by the City, the Seventh Circuit sought to reconcile its interpretation of the distinction between "judicial" and "statutory liens" with legislative history indicating that Congress intended for tax liens to qualify as "statutory liens." The City pointed out that federal tax liens result from judicial and quasi-judicial processes, such that under the Seventh Circuit's analysis in *Mance* they should technically qualify as "judicial" rather than "statutory liens," contrary to Congressional intent.

In a somewhat puzzling analysis, the Seventh Circuit conceded that "[t]ax liens are unquestionably statutory," but then suggested that the status of tax liens as statutory was not really a function of the definitions in the Bankruptcy Code and instead resulted from Congress's prerogative to "single out a particular category of liens and classify it." The Seventh Circuit's analysis on this point is arguably in tension with the general principle that statutory text should control over legislative history, because Congress "singled out" tax liens and "classified" them as statutory only in the legislative history. As such, the Seventh Circuit's interpretation of the Bankruptcy Code's statutory definitions of "judicial

lien" and "statutory lien" should arguably override that Congressional classification. Given that the status of tax liens was not directly at issue in *Mance*, however, the Seventh Circuit's statements on this issue are arguably not binding, and the exact status of tax liens in light of the *Mance* analysis may need to await a future decision.

Takeaways

In bankruptcy, holding a "statutory lien" can make all the difference between being a secured creditor entitled to payment in full and being an unsecured creditor entitled only to pennies on the dollar (if that). And yet, as *Mance* illustrates, whether a particular lien qualifies as a "statutory lien" can be a surprisingly fact-intensive question, notwithstanding the deceptive simplicity of the Bankruptcy Code's definitions. In particular, the fact that the final step in imposing the lien occurs by operation of statute may not be sufficient for the lien to qualify as a "statutory lien" if judicial or quasi-judicial proceedings preceded this final, statutory step.

Mance therefore serves as a reminder that municipal issuers and investors alike should engage in a careful and nuanced analysis of exactly what type of lien is likely to be created by a particular transaction before issuing or investing in municipal debt. *Mance* helpfully provides some additional guidance on this issue, but is likely far from the final word on the matter.

FOOTNOTES

1 See 11 U.S.C. § 552(a) ("[P]roperty acquired by the estate or by the debtor after the commencement of the case is not subject to any lien resulting from any security agreement entered into by the debtor before the commencement of the case").

2 See Ingrid Bagby, Michele C. Maman, Casey John Servais, & Eric G. Waxman, Stand Pat, Don't Act: U.S. Supreme Court Holds that Mere Retention of Debtor Property Does Not Violate Bankruptcy Code Section 362(a)(3), Pratt's Journal of Bankruptcy Law (April/May 2021), available at https://www.cadwalader.com/uploads/media/Pratt_reprint_cadwalader.pdf.

Tuesday, May 3, 2022

Financial Accounting Foundation Board of Trustees: Notice of Meeting

Meeting Notice

05/03/22

Puzzling Pieces: Component Unity Identification, Classification, Disclosure, and Display - GFOA

Although the basic shape of the financial reporting entity for state and local governments has been around for nearly 30 years, the Governmental Accounting Standards Board (GASB) has made many incremental changes over time. Most recently, GASB Statements No. 84, *Fiduciary Activities*, No. 90,

Majority Equity Interests, and No. 97, *Certain Component Unit Criteria*, and Accounting and Financial Reporting for Internal Revenue Code Section 457 Deferred Compensation Plans have introduced such changes. So, it is not terribly surprising that governments sometimes struggle to determine which entities should be included in a set of basic financial statements prepared in accordance with generally accepted accounting principles (GAAP), how they should be reported, and how both determinations should be explained.

DOWNLOAD

Government Finance Officers of America

Publication date: April 2022

Author: Michele Mark Levine

West Virginia Blasts S&P ESG Scoring as 'Politically Subjective'

- **The rating company's ESG scorecard debuted at end of March**
- **Republicans, industry groups have opposed more ESG oversight**

West Virginia's Republican treasurer called on S&P Global Ratings to scrap a new system scoring U.S. states on their environmental, social and governance efforts, calling the ratings scale a "politically subjective" scheme that will force states to yield to "woke capitalists."

"This new ESG rating system is just the beginning of a new wave of judging states – and their people – not by valid financial metrics, but by the preferred political views and outcomes of a select global elite," West Virginia State Treasurer Riley Moore said in a statement released earlier this week. "The ESG movement is nothing but a slippery slope whereby our states and our people will be forced to bend the knee to the woke capitalists or suffer financial harm."

Moore's condemnation follows a similar rebuke from Utah officials and comes amid a broader culture-war brawl between Republicans and corporate America. Texas has threatened to ban state investments in businesses that cut ties with oil and gas companies because of ESG initiatives. Florida has stripped Walt Disney Co. of some of its self-governance privileges after the company objected to a new law that limits school instruction about gender identity and sexual orientation.

S&P's new system scores governments on categories like human rights, social integration, low-carbon strategies, climate measures and sustainable finance. The company released its first scorecard March 31.

S&P declined to comment.

West Virginia, a Republican-controlled state, received a negative social score and a moderately negative environmental score. The vast majority of states' ratings were neutral. West Virginia has an AA- bond rating from S&P, its fourth-highest.

"So despite our state's excellent financial position, our taxpayers could now be punished with higher borrowing costs simply because S&P doesn't like our state's industries and demographic profile," Moore said. "This ratings scheme will affect our state and its municipalities, and begs the question: at what point will this stop? Will individuals soon get ESG ratings as part of their credit scores?

Where will it end?”

Institutional investors like BlackRock Inc. and pension funds are demanding greater clarity from companies on their efforts to diversify their workforces and address a changing climate. Meanwhile, GOP lawmakers and powerful industry groups, including the U.S. Chamber of Commerce, have opposed increased activity by financial watchdogs on ESG issues.

Bloomberg Markets

By Skylar Woodhouse

April 27, 2022

Some States’ Anti-ESG Push Garners Support In Congress.

Republican Congress could use riders to block SEC actions

Republican state lawmakers are berating U.S. financial institutions for increased reliance on environmental, social and governance metrics to screen investments and analyze credit risk factors, with some of the critics attracting support in Congress.

Utah state Treasurer Marlo Oaks coordinated a response to S&P Global Inc., blasting the financial services firm’s credit rating division for plans to supplement its analysis of states with a score on certain ESG indicators, such as exposure to climate risk and demographic trends.

While S&P notes the ESG analysis is added only after it issues the credit rating, the move nonetheless sparked backlash from the state’s GOP lawmakers, who say the inclusion of those factors stray from traditional financial factors.

“To call them ‘credit indicators’ attempts to legitimize a dubious and unproven exercise in developing a political ratings system that is based on indeterminate factors,” the letter said. “Traditional public finance entity credit ratings already incorporate financially material factors, including ESG factors.”

Notably, Oaks was joined by Gov. Spencer J. Cox, other state officials, and Utah’s entire congressional delegation: Republican Sens. Mitt Romney and Mike Lee and Reps. John Curtis, Blake D. Moore, Burgess Owens and Chris Stewart.

Stewart said he and his colleagues are encouraging other GOP members to have similar conversations with their state treasurers and financial regulators on the proliferation of ESG metrics.

If Republicans take back control of the House at the midterm elections, they will look to utilize appropriation riders to curb additional ESG regulations. This would be akin to the long-standing rider that prevents the Securities and Exchange Commission from pursuing rulemaking on corporate political spending disclosure, he said in an interview Tuesday.

“We’re going to be able to put some limits on this, precluding the Securities and Exchange Commission, for example, from using their regulatory authority to implement policies that are really out of bounds of their actual authority,” said Stewart, who sits on the House Appropriations Committee. “We’ll have some ability to push back on that starting next winter.”

The letter and Stewart's remarks underscore the latest effort from Republican politicians who are pushing back against the financial sector's embrace of ESG metrics in credit analysis and investment decisions.

In particular, leaders in fossil fuel producing states have pursued policies to bar officials from dealing with businesses that are moving to ditch fossil fuels or considering climate change in their own investments.

Last month, Texas Comptroller Glenn Hegar sent letters to nearly 20 banks and financial services providers asking if their funds either limit or block fossil fuel investments in light of a law to boycott investment vehicles divesting from oil, gas and coal firms — ultimately affecting Texas' pension funds. In West Virginia, the state dropped BlackRock Inc. funds from its portfolio over the asset manager's embrace of ESG investing.

Model policy

Earlier this month, the American Legislative Exchange Council released a model policy titled the State Government Employee Retirement Protection Act that's aimed to "protect pensioners from politically driven investment strategies."

The conservative organization — whose members consist of nearly one-quarter of the country's state legislators representing more than 60 million Americans — says ESG-oriented strategies in investments shrink investment returns over the long run, hurting retirees and taxpayers.

Under the policy framework, plan sponsors for state and local pension funds must evaluate investments only on pecuniary issues, defined as a factor with a material effect on financial risk or returns on investments. ESG factors and "similarly oriented considerations" are considered pecuniary factors "only if they present economic risks or opportunities that qualified investment professionals would treat as material economic considerations under generally accepted investment theories."

Investor advocacy groups and ESG supporters say that Republicans' criticisms and actions to fight the movement are misplaced, particularly on climate risk.

"We fundamentally reject the argument that ESG is not materially impactful," said Steven Rothstein, managing director of the Ceres Accelerator for Sustainable Capital Markets. Ceres is a nonprofit organization for investors concerned with sustainability and other ESG issues.

"There is lots of data that shows" ESG is material, he said in an interview. "There is also data that shows that companies that address these issues over the long term do better financially. Because they think about these constituencies."

While Rothstein said not every ESG issue has the same level of materiality, investors' sentiment shows physical and transitional risks from climate change and other topics will have an impact on the returns of their portfolios. State and federal officials who choose to exclude or ignore ESG factors may put pension funds and investments of Americans' money at risk.

"I wouldn't put this in the context of being supportive of ESG. It's supportive of their fiduciary responsibility to look at the range of financial risks," Rothstein said. "As someone had said three years ago, is the pandemic an ESG issue? Is it a public health issue? Or is it a financial risk issue? Well, it's all of them. And I don't think anyone would argue the pandemic hasn't had a dramatic impact on our economy, in lots and lots of ways."

Bryan McGannon, director of policy and programs at US SIF: The Forum for Sustainable and Responsible Investment, echoed similar sentiments that some states' pension plans may be misguided by blatantly ignoring certain ESG factors. US SIF is composed of advisers, firms and banks that support sustainable investing.

Depending on midterm results, Republicans may push for more oversight on what the SEC does on ESG regulations and bring forward more bills that challenge the inclusion of non-traditional financial metrics, McGannon said in an interview.

Such actions would be similar to what Republicans pursued in previous sessions of Congress when they controlled both chambers. Moreover, he said they would do little to change investors' overall sentiment that ESG factors are on equal footing with other financial factors.

"Frankly, it's more a political move," he said in an interview. "The marketplace is so far down the road that there is no going back."

Roll Call

By Ellen Meyers

April 28, 2022

SEC Chief Floats Slashing Bond-Trade Reporting to 1 Minute.

- **Gensler sees benefit in cutting current 15-minute window**
- **Transaction data sent to Trace should also be broader, he says**

U.S. Securities and Exchange Commission Chair Gary Gensler wants to slash the amount of time that traders have to report many bond transactions as part of a bid to increase visibility into fixed-income markets.

Gensler on Tuesday said that more transparency was needed across global bond markets, and that disclosures had generally failed to keep up with technological changes. In remarks for City Week in London, the SEC chief said data should be sent faster to the Financial Industry Regulatory Authority's Trace reporting system and cover more types of securities.

"Currently, a trade has to be reported as soon as practicable but no later than within 15 minutes of the time of execution," he said, also referring to how transactions involving municipal securities are reported to regulators. "Why couldn't the outer bound be shortened to no later than, for example, 1 minute?"

The amount of time that traders have to report fixed-income transactions has been a hot-button issue for regulators since before Gensler took over the last April. During the Trump era, a controversial plan to test whether delaying disclosure of the biggest corporate bond trades would boost market liquidity was eventually shelved after strong industry opposition.

Gensler said there could also be value in broadening Trace reporting to include sovereign debt transactions. The market impacts of Russia's invasion of Ukraine "have shown the value that regulatory reporting and public dissemination of foreign sovereign bonds would offer."

A Finra spokesman said the watchdog was supportive of Gensler's plans. However, financial firms

will still have a chance to weigh in as any proposal would have to wind through a byzantine rule-making process that includes approval by the SEC, which oversees the industry-backed regulator.

Other potential measures for boosting transparency could include making public Trace data on individual Treasury transactions, Gensler suggested. Authorities could look into reporting trading protocols and fees paid for transactions, as well as the "spread" to Treasuries when the trade is agreed upon, he said.

Shortening the reporting time for fixed-income securities would involve a transition that "could take quite a bit of time," said Gennadiy Goldberg, a U.S. rates strategist at TD Securities.

"The timing of trade reporting is a delicate balancing act between creating sufficient transparency and creating so much transparency that buyers and sellers have trouble executing their positions without being revealed to markets in the process," Goldberg added.

Bloomberg Markets

By Lydia Beyoud

April 26, 2022

— With assistance by William Shaw, and Tom Metcalf

MSRB Votes to Seek Public Comment on Enhancing Post-Trade Transparency at Quarterly Board Meeting.

Washington, DC – The Municipal Securities Rulemaking Board (MSRB) met April 26-28, 2022 for its quarterly Board of Directors meeting, where the Board determined to seek public comment on enhancing post-trade transparency and to continue to foster dialogue on environmental, social and governance (ESG) practices in the $4 trillion municipal market, among other initiatives to advance the four goals outlined in its long-term strategic plan.

The Board met with Securities and Exchange Commission (SEC) Chair Gary Gensler. The Board regularly meets with SEC officials and the leadership of other self-regulatory organizations in support of regulatory coordination and communication.

"As we fully expected at the start of the fiscal year, this Board has worked thoughtfully and collaboratively to advance one of the most impactful and consequential agendas in our history," said MSRB Chair Patrick Brett. "At our third meeting of the year, we were honored to speak with Chair Gensler about how the policy priorities of the Commission intersect with our work to engage constructively with municipal market stakeholders to further our mission to strengthen and protect the municipal market."

Regulatory Initiatives

The Board will seek public comment on a retrospective review of MSRB Rule G-14, the rule that since 2005 has ensured investors and the public have access to trade prices within 15 minutes of the time of trade on the free Electronic Municipal Market Access (EMMA®) website.

"As part of our focus on modernizing our rule book in light of evolving market practices and

technology, we are interested in exploring whether the time might be right to consider shortening what constitutes 'real-time' trade reporting in our unique market," said MSRB CEO Mark Kim. "We plan to solicit public comment from dealers, investors and other stakeholders about the benefits and challenges of potential rule amendments to enhance post-trade transparency."

Transparency Initiatives

The Board previewed the future-state MSRB.org website, which is being redesigned with the benefit of extensive input from stakeholders to make MSRB rules, compliance resources, educational materials and other information easier and more intuitive to find. The new MSRB.org, which is planned to be implemented this year, also is designed to complement the ongoing work to modernize the EMMA website and related market transparency systems.

To help keep stakeholders informed of upcoming and longer-term EMMA enhancements, the MSRB publishes a forward roadmap of its transparency and technology initiatives on its website.

Market Structure and Data

Also at its meeting, the Board was briefed on structured data, including pending federal legislation and the emerging use of structured data in the municipal market.

"The Board was briefed on legislation and activities at the federal, state and local level to move toward open data, and we discussed the potential to showcase state and local leadership on this front, and innovate collaboratively on our EMMA Labs platform," Brett said.

The MSRB this year launched EMMA Labs as an innovation sandbox to collaborate with market participants to advance transparency and the quality and comparability of data in the municipal securities market.

Public Trust

In support of its commitment to uphold the public trust and stay engaged with the market about evolving trends, the Board in December invited the public to share information and perspectives on environmental, social and governance (ESG) practices in the municipal securities market.

As a next step, the MSRB plans to prepare and publish a summary of the diverse comments received on its request for information on ESG practices in the municipal market. The MSRB also plans to host a series of virtual town halls to further explore the various themes raised by commenters.

"We are pleased that so many different organizations and individuals took advantage of our 90-day comment period to share their perspectives on this evolving and growing area of our market," said MSRB Vice Chair Meredith Hathorn. "As the Board continues to synthesize the wealth of information provided, we have many threads to pull, including specific suggestions to enhance the EMMA website. We look forward to continuing to provide forums to bring different viewpoints together for more dialogue."

Date: April 29, 2022

Contact: Leah Szarek, Chief External Relations Officer
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MSRB Proposes to Extend SEC's Regulation Best Interest to Bank Dealers.

The Municipal Securities Rulemaking Board today proposed a rule change that would amend an existing rule on the suitability of recommendations and transactions. The proposed changes would promote regulatory parity between bank dealers and broker-dealers with regard to Regulation Best Interest and the recommendation of municipal securities transactions or investment strategies involving municipal securities.

The MSRB also proposed changes to another rule related to transactions with sophisticated municipal market professionals. The changes are subject to approval by the Securities and Exchange Commission.

In previous comments, the American Bankers Association has urged the MSRB to consider the compliance costs of including bank dealers in the SEC's Regulation Best Interest Rule, noting that bank dealers in municipal securities do not have a significant retail customer base to warrant a new regulatory compliance regime.

ABA BANKING JOURNAL

APRIL 19, 2022

April 2022 MSRB Board of Directors Meeting Discussion Items.

The Board of Directors of the Municipal Securities Rulemaking Board (MSRB) will meet in Washington, D.C. on April 26-28, 2022, where it will discuss the following topics:

Market Regulation

The Board will discuss seeking public comment on a retrospective review of MSRB Rule G-14 to modernize trade reporting requirements with a view to enhancing post-trade transparency.

Market Transparency

The Board will preview the future-state MSRB.org website, which is being redesigned to make MSRB rules, compliance resources, educational materials and other information easier and more intuitive to find, and to complement the ongoing work to modernize the Electronic Municipal Market Access (EMMA®) website and related market transparency systems.

Market Structure and Data

The Board will discuss potential new opportunities to collaborate with market participants in EMMA Labs, the MSRB's innovation sandbox, to advance transparency and the quality and comparability of data in the municipal securities market.

Public Trust

As part of its commitment to uphold the public trust and serve as a forum for conversation about evolving municipal market matters, the Board published a request for information on environmental, social and governance (ESG) practices in the municipal securities market in December 2021.

Following the end of the 90-day comment period in March, the Board began its review of comments received and will discuss preliminary themes at its meeting.

April Edition of GFOA Government Finance Review Now Available.

The April edition of GFR is now available to read digitally. Rethinking Local Government Revenue is among the many articles this month. We know changes to the revenue systems in local government are necessary, but how do local governments evaluate options and initiate transformation?

READ GFR ONLINE

MSRB to Discuss ESG Request for Information at Quarterly Meeting.

The Municipal Securities Rulemaking Board intends to discuss the preliminary themes in the comments it received as part of its request for information on environmental social and governance factors, in its first meeting since the comment period closed in March.

The board will discuss that along with the efforts to update trade reporting rules in its Rule G-14, as well as updates to its websites during the board's quarterly meeting on April 26-28.

The board's request for information on ESG has provoked concern from many market participants, with some saying the MSRB overstepping its reach. But the response has varied from criticizing the way in which the board framed its questions to accusations that the board is politicizing public finance.

The meeting marks the first time since the board closed its comment period in March that the members will discuss the comments and their preliminary themes.

The board will continue its efforts to improve transparency in the municipal securities market, whether through its own systems or through rules for other market participants, according to its agenda.

"The board will discuss seeking public comment on a retrospective review of MSRB Rule G-14 to modernize trade reporting requirements with a view to enhancing post-trade transparency," the MSRB said.

The MSRB.org website is being redesigned in order to make "MSRB rules, compliance resources, educational materials and other information easier and more intuitive to find," the MSRB said, in addition to making it a more seamless complement to its EMMA website.

The MSRB launched its EMMA Labs platform at the top of this year to enhance and accelerate the use of data analytics in the municipal securities market, and the board will use its upcoming meeting to discuss new opportunities for collaboration with market participants.

The efforts surrounding EMMA Labs will hope to "advance transparency and the quality and comparability of data in the municipal securities market," the board said.

By Connor Hussey

BY SOURCEMEDIA | 04/21/22

Utah Officials Blast S&P Over ESG Credit Indicators.

Utah's top elected officials demanded on Thursday that S&P Global Ratings cease applying environmental, social, and governance factors to the state through the use of what they called a politicized rating system based on indeterminate factors.

A letter to S&P signed by Gov. Spencer Cox, Treasurer Marlo Oaks, other state constitutional officeholders, legislative leaders, and Utah's Congressional delegation, stated their objection "to any ESG ratings, ESG credit indicators, or any other ESG scoring system that calls out ESG factors separate from, in addition to, or apart from traditional credit ratings."

S&P, which rates Utah AAA with a stable outlook, declined to comment about the letter.

In an ESG credit indicator report card for all 50 states that S&P released on March 31, Utah was assigned "a moderately negative" score for environmental factors, due largely to long-term water supply challenges. Cox declared a state of emergency on Thursday due to "dire drought conditions affecting the entire state."

The state received neutral scores for social and governance factors.

The letter demanded that S&P withdraw those credit indicators and stop publishing any ESG factors for the state.

"Considering recent global events, the current economic situation in the U.S., and the unreliability and inherently political nature of ESG factors in investment decisions, we view this newfound focus on ESG as politicizing the ratings process," the letter stated. "It is deeply counterproductive, misleading, potentially damaging to the entities being rated, and possibly illegal."

It added that "no financial firm should substitute its political judgments for objective financial analysis, especially on matters that are unrelated to the underlying businesses, assets and cash flows it evaluates."

The elected officials also expressed concern "the disclosure of ESG factors will unfairly and adversely affect Utah's credit rating and the market for Utah's bonds, especially where the alleged indicators are not indicative of Utah's ability to repay debt."

Oaks, who spearheaded a response signed by officials from 23 states to the Municipal Securities Rulemaking Board's request for information on ESG considerations in the municipal market, called Utah's AAA rating an important asset to the state.

"I'm grateful for the unified approach our leaders have taken in pushing back against S&P's move to politicize the ratings process, which ultimately threatens our outstanding credit and, more broadly, our pluralistic systems of free-market capitalism and democracy," he said in a statement.

A Bond Buyer survey last year showed 56% of respondents rated ESG as important to the municipal industry, although only 42% said it is important for rating agencies to take ESG into consideration for ratings. Two-thirds of respondents said it was very important or critical for issuers to disclose ESG risks and opportunities.

Matt Fabian, a partner at Municipal Market Analytics, said the “genie is out of the bottle.”

“Because few state and local governments have decided to provide solid data on their credit exposure to climate change, investors are relying on data from third party providers that, by definition, the states don’t control,” he said. “As the science gets better, and third-party data changes, gets smarter, and becomes more predictive and invasive, it’s only going to get worse for states trying to manage what investors see.”

In its March report card, S&P said the ESG credit indicators “provide additional disclosure and transparency at the entity level and reflect our opinion of the influence that environmental, social, and governance factors have on our credit rating analysis. They are applied after the credit rating has been determined.”

ESG ratings criteria published by S&P in October noted it was looking at factors that can materially influence an issuer’s creditworthiness and that if factors are sufficiently material they can influence credit ratings.

The Utah letter, which was addressed to S&P Global Ratings President and CEO Douglas Peterson and President Martina Cheung, included a list of detailed questions regarding S&P’s consideration of ESG factors in public finance credit ratings, as well as a description of any communications it has had with the U.S. Securities and Exchange Commission, the MSRB, the U.S. Treasury Department, or any other governmental agency regarding the use of ESG factors for credit ratings.

Brittany Griffin, Oaks’ spokeswoman, said other rating agencies have not gone as far as S&P in their use of ESG credit indicators.

Fitch Ratings, Moody’s Investors Service, and Kroll Bond Rating Agency also look at ESG factors in their ratings. Moody’s and Fitch have scoring systems, while KBRA has an ESG Management System that does not provide scores, but if an ESG factor is relevant to credit, the factor is incorporated into its analysis in the same manner as all other relevant factors across KBRA’s rated sectors.

By Karen Pierog

BY SOURCEMEDIA | 04/22/22

SEC Charges School District, the District’s Former Chief Financial Officer and the District’s Auditor with Violations of Federal Securities Laws in a 2018 Bond Offering.

On March 16, 2022, the Securities and Exchange Commission (“SEC”) entered an order against a school district (Crosby Independent School District (the “District”), located in a suburb of Houston, Texas) and against the District’s auditor (the “Auditor”) and charged the school district’s former chief financial officer (“CFO”) with misleading investors who purchased $20 million of the District’s 2018 bonds (the “Bonds”).

In its actions, the SEC noted that the District, the CFO and the Auditor included false and misleading audited financial statements in the official statement for the Bonds. Specifically, the FY2017 financial statements underreported construction liabilities (by $7.9 million) and payroll expenses (by $3.8 million) resulting in the financial statements overstating the general fund balance by $11.7 million. The District submitted the FY2017 financial statements for use with the offering document,

the District and the CFO reviewed the offering document prior to its use in marketing the Bonds, and the school board's president signed the offering document. The District changed its fiscal year end as part of a plan to address the District's financial condition prior to offering the Bonds, and the change in fiscal year end should have prompted a heightened level of scrutiny on the Auditor's part. The SEC determined that the Auditor's audit procedures were deficient.

The District. The charges against the District were brought under the Securities Exchange Act of 1934 ("1934 Act") Section10(b) and Rule 10(b)(5) thereunder and the Securities Act of 1933 ("1933 Act") Section 17(a). Violations of 1933 Act Section 17(a) do not require intentional wrongdoing on the part of the actor and can be established on the basis of negligence. The SEC's order against the District found that it violated 1934 Act Section 10(b) and Rule 10b-5 thereunder and 1933 Act Section 17(a). The District was ordered to cease and desist from committing or causing any violations and any future violations of 1934 Act Section 10(b) and Rule 10b-5 and 1933 Act Section 17(a).

The CFO. The SEC alleged the CFO violated 1933 Act Section 17(a)(1) and (3) and 1934 Act Section 10(b) and Rule 10b-5. The CFO has agreed to settle with the SEC, including paying a $30,000 penalty and not participating in any future municipal securities offerings. The settlement is pending court approval.

The Auditor. The SEC's order against the Auditor found that she engaged in improper professional conduct pursuant to 1934 Act Section 4C(2) and SEC Rules of Practice Rule 102(e)(1)(ii). The SEC's order was effective immediately and denied the Auditor the privilege of appearing or practicing before the SEC as an accountant.

A similar recent case. This set of cases follows SEC actions from September 2021 involving a California school district and its CFO wherein that California school district included misleading budget projections in its offering documents for its bonds due to the budget's failure to reflect salary increases. Despite reports showing actual expenses were higher than projected, the California school district used the stale information and the CFO attested to the accuracy of the information in the offering document. The SEC order against the California school district found that it violated 1933 Act Section 17(a)(2) and (3) by "making misleading statements and omissions to investors, as well as to the bonds' credit rating agency and other municipal industry professionals on the transaction." The California school district was ordered to cease and desist violating 1933 Act Section 17(a)(2) and (3), implement various written policies and procedures, conduct staff training, retain an independent consultant to review the policies and procedures, implement recommendations of the independent consultant, disclose this settlement in future bond offerings, and provide certifications of compliance to the Staff of the SEC regarding these settlement conditions. The SEC charged the former CFO with violating 1933 Act Section 17(a)(3).

Dorsey & Whitney LLP

April 15, 2022

SEC Proposes Significant Expansion of Firms That Must Register as Dealers: Sidley

On March 28, 2022, the U.S. Securities and Exchange Commission (SEC) unanimously proposed rules to further define activity that requires registration as a "dealer" or "government securities

dealer" with the SEC (the Proposal).1 The Proposal would generally require any person, which would include a natural person or legal entity, that engages in a routine pattern of buying and selling securities (or government securities) that has the effect of providing liquidity to other market participants to have to register as a dealer pursuant to Section 15(b) of the Securities Exchange Act of 1934, as amended (the Exchange Act) (or as a government securities dealer pursuant to Section 15C of the Exchange Act).

Specifically, the SEC is proposing two rules — Proposed Rules 3a5-4 and 3a44-2 under the Exchange Act — to further define what it means to trade securities or government securities for one's own account "as part of a regular business" in a manner that would require a person to register as a "dealer" or a "government securities dealer," respectively, absent an exception or exemption (other than the so-called "trader" exception/exemption from such definitions).2

According to the SEC, the impetus for the Proposal is advancements in electronic trading and technology across securities markets that have given rise to unregistered market participants (referred to as "proprietary trading firms") playing an increasingly significant "liquidity providing role" in overall trading and market activity.3 Alleging that certain of these unregistered liquidity-providing firms are performing traditional "dealer" activity, the SEC is concerned that an uneven playing field has developed where some market participants are subject to regulation and others are not. This uneven application of regulatory oversight, according to the SEC, makes it difficult for regulators to detect, investigate, and understand significant market events, such as the "flash rally" in the Treasury markets in October 2014.

Hedge fund managers that actively trade will need to carefully consider whether they fall within the scope of the proposed rules and would therefore have to register as a dealer (or government securities dealer). If so, such hedge funds would face immensely greater regulatory scrutiny and compliance costs as they would become subject to SEC rules (e.g., net capital requirements, increased recordkeeping, risk management), self-regulatory organization rules (e.g., trade reporting, self-reporting of rule violations), and increased examinations and enforcement investigations.

The Proposal's comment deadline is the later of (i) Friday, May 27, 2022 (60 days after issuance of the Proposal), or (ii) 30 days after publication of the Proposal in the *Federal Register*.

Background

Section 3(a)(5)of the Exchange Act generally defines the term "dealer" to mean "any person engaged in the business of buying and selling securities … for such person's own account through a broker or otherwise" but excludes "a person that buys or sells securities … for such person's own account, either individually or in a fiduciary capacity, but not as a part of a regular business."4 This statutory exclusion from the definition of "dealer" is often referred to as the "trader" exception.5

According to the SEC, while traders and dealers engage in the same core activity — buying and selling securities for their own account — their level of activity varies in absolute terms and in regularity. For example, the SEC has stated that dealers often buy and sell contemporaneously and quickly enter into offsetting transactions to minimize the risk associated with a position.6 In contrast, the SEC has said that traders are "market participants who provide capital investment and are willing to accept the risk of ownership in listed companies for an extended period of time" and that " it makes little sense to refer to someone as 'investing' in a company for a few seconds, minutes, or hours."7

The SEC last indicated that it might consider a rulemaking related to distinguishing a dealer from a trader in 2014 when the then-Chair of the SEC announced, as part of a number of other market

structure initiatives, that she had asked the staff to recommend a rulemaking to "clarify the status of unregistered active proprietary traders to subject them to [SEC] rules as dealers."8 However, the SEC did not promulgate a proposal until now.

Further Definition of "As Part of a Regular Business"

The operative concept in the definitions of "dealer" and "government securities dealer" that distinguishes the regulated entity from the unregulated trader is that the dealer is engaged in buying and selling securities for its own account "as part of a regular business." Accordingly, the Proposal is designed to further define what "as part of a regular business" means by defining three qualitative standards intended to more precisely identify activities of certain market participants who assume dealerlike roles. Specifically, the proposed new rules seek to identify persons whose trading activity in the market "has the effect of providing liquidity" to other market participants.

Under the proposed rules, a person would be engaged in buying and selling securities (or government securities)9 for its own account "as a part of a regular business" if that person engages in a "routine pattern" of buying and selling securities (or government securities) that has the effect of providing liquidity to other market participants by

1. Routinely10 making roughly comparable11 purchases and sales of the same or substantially similar12 securities in a day;13
2. Routinely expressing trading interests14 that are at or near the best available prices on both sides of the market and that are communicated and represented in a way that makes them accessible to other market participants; or
3. Earning revenue primarily from capturing bid-ask spreads, by buying at the bid and selling at the offer, or from capturing any incentives offered by trading venues to liquidity-supplying trading interests.15

For persons buying and selling government securities, there would be an additional quantitative standard that, if met, would automatically deem the person to be engaging in the activity "as part of a regular business," irrespective of whether the person meets any of the other qualitative criteria. Under this standard, a person engaged in buying and selling more than $25 billion of trading volume in government securities in each of four of the last six calendar months would be deemed to be doing so "as part of a regular business."16

Notably, the proposed rules relate only to the interpretation of the Exchange Act's "dealer" and "government securities dealer" definitions under Sections 3(a)(5) and 3(a)(44) of the Exchange Act, respectively. The SEC is not proposing a comparable rule with respect to the Exchange Act's "municipal securities dealer" definition under Section 3(a)(30) of the Exchange Act or "security-based swap dealer" under Section 3(a)(71) of the Exchange Act.

There would not be a presumption that a person is not a dealer (or government securities dealer) solely because that person does not satisfy (1), (2), or (3) above.17

Exclusions From the Proposed Rules; Intersection of the Proposed Rules With Other Exceptions and Exemptions

The proposed rules would exclude two specific categories of persons from their coverage — meaning that if a person meets the criteria noted above but falls within an exclusion, such person's activities would not — by virtue of these criteria alone — be deemed to be "part of a regular business." The exclusions are for a person that

1. Has or controls total assets of less than $50 million or
2. Is an investment company registered under the Investment Company Act of 1940.18

Because there is no presumption under the proposed rules that a person is not a dealer (or government securities dealer) if not meeting the relevant criteria described above, market participants would still need to analyze their activity under prior SEC guidance and precedent, and applicable case law, to determine whether the activities may otherwise implicate the dealer and/or government securities dealer definitions.19

The proposed rules also would not change other available statutory or regulatory exceptions or exemptions that may be available to a particular person. For example, banks would continue to enjoy the various bank-specific exceptions and exemptions from the "dealer" and "government securities dealer" definitions.20 Moreover, even if a person is deemed to implicate the "dealer" and/or "government securities dealer" definitions, an exemption from the requirement to register may remain available — such as the exemption for foreign broker-dealers complying with Rule 15a-6 under the Exchange Act.21

Aggregation of Accounts Under the Proposal

To account for variations in corporate structure and ownership among different persons, and to prevent possible circumvention of the proposed rules, the Proposal would also define the terms "own account" and "control." The proposed definitions are designed to determine which accounts must be considered for purposes of evaluating whether a person meets the criteria described above. Specifically, a person's "own account" would be defined to mean any account

1. held in the name of that person,
2. held in the name of a person over whom that person exercises control or with whom that person is under common control (subject to certain exceptions, as discussed below), or
3. held for the benefit of those persons identified in (i) and (ii).

Exception for Certain Accounts

The Proposal sets forth certain exceptions under prong (ii). Specifically, an account held in the name of a person over which the person exercises control or with whom the person is under common control would not be considered for purposes of determining whether the person may be a dealer/government securities dealer if the account meets one of the following exceptions:

(A) Broker-Dealer and Investment Company Accounts — The account is in the name of a registered broker, dealer, or government securities dealer or an investment company registered under the Investment Company Act of 1940.

(B) Investment Advisory Accounts for Clients That Are Not Controlled by the Adviser — With respect to an investment adviser registered under the Investment Advisers Act of 1940 (Advisers Act), the account is held in the name of a client of the adviser (unless the adviser controls the client as a result of the adviser's right to vote or direct the vote of voting securities of the client, the adviser's right to sell or direct the sale of voting securities of the client, or the adviser's capital contributions to or rights to amounts upon dissolution of the client).22

(C) Accounts for Shared Clients of an Adviser (Other than Parallel Account Structures) — With respect to any person, the account is held in the name of another person that is deemed under common control with that person solely because both persons are clients of an investment adviser registered under the Advisers Act (an RIA), unless the accounts constitute a "parallel account

structure."

Under the Proposal, the term "control" would have the same meaning as prescribed in Rule 13h-1 (Large Trader Reporting) under the Exchange Act, which generally presumes control at a level of 25% interest.23

The term "parallel account structure" would be defined to mean "a structure in which one or more private funds (each a 'parallel fund'), accounts, or other pools of assets (each a 'parallel managed account') managed by the same investment adviser pursue substantially the same investment objective and strategy and invest side by side in substantially the same positions as another parallel fund or parallel managed account."24

Investment Advisers Under the Proposal

RIAs would be subject to the proposed rules.25 The SEC states that an RIA could become subject to the proposed rules with respect to trading for its own proprietary account, as well as the accounts of clients the RIA controls, unless an exclusion or exemption applies. Importantly, the fact that the RIA has discretionary authority over a client's account would not itself cause the account's trading activity to be aggregated with the activity for the RIA's own proprietary account. Rather, aggregation would be required only if the RIA controls the client itself.26

If the Proposal is adopted in its current form, RIAs will need to carefully consider which advisory clients are considered under their control and hence which clients' advisory accounts must be aggregated with the RIA's own proprietary account for purposes analyzing the RIA's activities under the proposed rules.

Dealer Registration With the SEC and Self-Regulatory Organizations

If adopted, any person deemed to be acting as a dealer (or government securities dealer) under the proposed rules would, absent an available exception or exemption or "no-action" position, have to register with the SEC and become a member of a national securities exchange and/or FINRA and comply with applicable SEC and exchange/FINRA rules within one year of the effective date of any final rules.27 Compliance with certain of these rules could prove challenging for some firms based on their current business model. For example, the SEC generally requires all registered broker-dealers to comply with its net capital rule under Rule 15c3-1 of the Exchange Act. The SEC's net capital rule, as well as certain FINRA rules, imposes substantial limitations/restrictions on the ability to withdraw capital from such broker-dealer, and FINRA or an exchange could impose limits/restrictions on the amount of leverage used by a broker-dealer. This could restrict liquidity for investors in a private investment/hedge fund that seeks to trade principally through a wholly owned subsidiary that is a registered broker-dealer.

While it is currently possible for certain exchange-member dealers to avoid FINRA membership, market participants would be wise to not expect the current exemption from FINRA membership to last. Section 15(b)(8) of the Exchange Act generally requires that a broker-dealer become a member of a national securities association (i.e., FINRA, as the sole-registered securities association), unless the broker-dealer effects transactions solely on an exchange of which it is a member.28 Rule 15b9-1 provides a further exemption from FINRA membership, generally allowing an exchange-member dealer that carries no customer accounts and effects all of its trades with or through other registered broker-dealers to avoid FINRA membership.29

In 2015, however, the SEC proposed amendments to significantly narrow the Rule 15b9-1 exemption from FINRA membership.30 It seems reasonable to expect that the SEC might repropose the

narrowing of this exemption in the coming months to ensure that dealers captured by the Proposal are subject to regulatory oversight by FINRA, as the primary regulator of the over-the-counter (OTC) markets. Exchanges are not well positioned to regulate and oversee the trading activity of, for example, a government securities dealer that transacts almost exclusively in the OTC treasury markets. Accordingly, we anticipate that proposed changes to Rule 15b9-1 may be forthcoming.

State "Blue Sky" Law Provisions Would Continue to Apply

The Proposal relates only to the interpretation of the Exchange Act's "dealer" and "government securities dealer" definitions. Individual state "Blue Sky" law provisions would continue to apply, although many states' Blue Sky laws contain provisions that require such laws to be interpreted to promote uniformity with other states' laws and the "related federal regulation." As such, generally, a person that is not deemed to be a dealer (or government securities dealer) under the Exchange Act should, as a general matter, not be subject to separate registration under state Blue Sky laws. However, to the extent that a person is required to be registered as a dealer (or government securities dealer) under the Exchange Act, the state Blue Sky laws do not separately regulate securities "dealers" versus "government securities dealers" but rather regulate "broker-dealers." In this regard, a broker-dealer could include both a securities dealer and a government securities dealer.

As a general matter, a person registered as a dealer or government securities dealer under the Exchange Act and which (i) does not maintain a place of business in a particular state and (ii) effects securities transaction in a state solely with certain enumerated categories of institutional investors (including one or more state-registered broker-dealers) would not be required to be separately registered as a broker-dealer under the applicable state's Blue Sky law. Even if a person is required to become registered under a state's Blue Sky laws, Section 15(i)(1) of the Exchange Act preempts the states from imposing requirements on an Exchange Act–registered dealer with respect to, among other things, capital, margin, keeping records, and financial and operational reporting requirements that "differ from, or are in addition to, the requirements in those areas established under [the Exchange Act]."31

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April 11, 2022

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1 Exchange Act Release No. 94524 (March 28, 2022), https://www.sec.gov/rules/proposed/2022/34-94524.pdf.
2 The Proposal does not address the definitions of "municipal securities dealer" in Section 3(a)(30) of the Exchange Act or "security-based swap dealer" in Section 3(a)(71) of the Exchange Act.
3 The SEC estimates that the Proposal would require approximately 51 persons to register as dealers and 46 persons to register as government securities dealers. Proposal at 171-172.
4 15 U.S.C. 78c(a)(5)(A) and (B). Similarly, Section 3(a)(44) of the Exchange Act provides, in relevant part, that the term "government securities dealer" means "any person engaged in the business of buying and selling government securities for his own account, through a broker or otherwise" but does not include "any person insofar as he buys or sells such securities for his own account, either individually or in some fiduciary capacity, but not as part of a regular business." 15 U.S.C. 78c(a)(44).
5 Exchange Act Release No. 46745 (Oct. 30, 2002), 67 FR 67496, 67498–67500 (Nov. 5, 2002) (explaining that "a person that is buying securities for its own account may still not be a 'dealer'

because it is not 'engaged in the business' of buying and selling securities for its own account as part of a regular business" and that "[t]his exclusion is often referred to as the dealer/trader distinction").

6 The SEC has identified a number of other indicators of dealer activity, including, among other things, (1) acting as a market maker or specialist on an organized exchange or trading system, (2) acting as a de facto market maker or liquidity provider, and (3) holding oneself out as buying or selling securities at a regular place of business.

7 Proposal at 21.

8 Former SEC Chair, Enhancing Our Equity Market Structure (June 5, 2014), https://www.sec.gov/news/speech/2014-spch060514mjw.

9 The SEC notes that the proposed rules would apply to any security or government security (as defined in Sections 3(a)(10) and 3(a)(42) of the Exchange Act, respectively), "including any digital asset that is a security or a government security within the meaning of the Exchange Act." See Proposal at n.36.

10 The Proposal states that "routinely" means "more frequent than occasional but not necessarily continuous" and that this interpretation of the term "will separate persons engaging in isolated or sporadic securities transactions from persons whose regularity of participation in securities transactions demonstrates that they are acting as dealers." Proposal at 48-49.

11 The Proposal states that "roughly comparable" means "similar enough, in terms of dollar volume, number of shares, or risk profile, to permit liquidity providers to maintain near market-neutral positions by netting one transaction against another transaction." Id. at 50. The SEC offers no bright-line test for "roughly comparable" but additionally states that "a person that closes or offsets, in the same day, the overwhelming majority of the positions it has opened, has likely made 'roughly comparable purchases and sales.' " Id.

12 With respect to the meaning of "the same or substantially similar," the Proposal states that securities are the "same" if they are "securities of the same class and having the same terms, conditions, and rights," such as securities with the same CUSIP. Id. at 52. Whether securities are considered to be "substantially similar" would be a facts and circumstances analysis, taking into account such factors as whether "(1) the fair market value of each security primarily reflects the performance of a single firm or enterprise or the same economic factor or factors, such as interest rates; and (2) changes in the fair market value of one security are reasonably expected to approximate, directly or inversely, changes in, or a fraction or a multiple of, the fair market value of the second security." Id. at 53.

13 This category would encompass "day trading" activity meeting this criteria — activity that has historically been regulated by self-regulatory organization margin rules, such as, Rule 4210(f)(8)(B) of the Financial Industry Regulatory Authority, Inc. (FINRA).

14 The Proposal states that the term "trading interest" is intended to capture "traditional quoting engaged in by dealer liquidity providers, new and developing quoting equivalents, and the orders that actually result in the provision of liquidity" that the SEC intends the proposed rules to address. Id. at 57.

15 See proposed Rules 3a5-4(a)(1) and 3a44-2(a)(1).

16 See proposed 3a44-2(a)(2).

17 See proposed Rules 3a5-4(c) and 3a44-2(c). See also Proposal at 35-37 and 94-95.

18 See proposed Rules 3a5-4(a)(2) and 3a44-2(a)(3).

19 For example, an entity that is acting as an underwriter would still be required to register as a dealer. Proposal at 94.

20 See, e.g., Exchange Act Sections 3(a)(5)(C) and 3(a)(44)(C).

21 17 CFR 240.15a-6. See Proposal at 29. Rule 15a-6 under the Exchange Act provides a "foreign broker or dealer" (as defined in the rule) a limited exemption from the registration requirements of Sections 15(a)(1) and 15B(a)(1) of the Exchange Act (that is, with respect to securities dealers and municipal securities dealers, but not government securities dealers). Treasury Regulation 401.7,

however, provides a substantially similar exemption with respect to the registration requirements in Section 15C(a) of the Exchange Act. 17 CFR 401.7.
22 Put another way, the fact that a registered investment adviser (RIA) has discretionary authority over a client's account would not itself cause the account's trading activity to be attributed to the investment adviser for purposes of the proposed rules. On the other hand, if the investment adviser is deemed to control the client, then the trading activity for that client account would be attributed to the investment adviser.
23 17 CFR 240.13h-1. Rule 13h-1(a)(3) provides that "the term control (including the terms controlling, controlled by and under common control with) means the possession, direct or indirect, of the power to direct or cause the direction of the management and policies of a person, whether through the ownership of securities, by contract, or otherwise. For purposes of this section only, any person that directly or indirectly has the right to vote or direct the vote of 25% or more of a class of voting securities of an entity or has the power to sell or direct the sale of 25% or more of a class of voting securities of such entity, or in the case of a partnership, has the right to receive, upon dissolution, or has contributed, 25% or more of the capital, is presumed to control that entity."
24 See proposed Rules 3a5-4(b)(4) and 3a44-2(b)(4).
25 Although there is an exclusion from the definition of "investment adviser" for any broker or dealer whose performance of advisory services is solely incidental to the conduct of such person's business as a broker or dealer, and who receives no special compensation therefor (see Section 202 (a)(11)(C) of the Advisers Act), there is no comparable exception from the definition of "dealer" (or " broker") under the Exchange Act for an RIA.
26 See also note 22, supra.
27 The compliance period would apply only to persons captured by the proposed rules as of the effective date of any final rules but would not cover market participants whose activities are captured by the final rules only after the effective date. Proposal at 34-35. This compliance period could prove challenging as, for example, it can take six months or longer to become a FINRA member.
28 15 U.S.C. 78o(b)(8).
29 17 CFR 242.15b9-1. Rule 15b9-1 generally exempts a broker-dealer from the requirement to become a member of a national securities association if it is a member of a national securities exchange, carries no customer accounts, and has annual gross income of no more than $1,000 that is derived from securities transactions effected otherwise than on a national securities exchange of which it is a member. Under the rule, income derived from transactions for the dealer's own account with or through another registered broker-dealer does not count toward this $1,000 de minimis threshold.
30 Exchange Act Release No. 74581, 63 FR 18036 (Apr. 2, 2015).
31 15 U.S.C. 78o(i)(1)

Q1 2022 Update on LIBOR Transition Developments: McGuireWoods

Since passing the December 31, 2021 "no new LIBOR" line-in-the-sand drawn by regulators, the pace of new developments in LIBOR transition has slowed as various markets have adapted to pricing transactions at SOFR or some other alternative to LIBOR. As we close out Q1 2022, here are some of the highlights in events and trends we've seen since our last post.

Federal LIBOR Legislation: On March 15, 2022, President Biden signed the Consolidated Appropriations Act, 2022, which contains as part of its many provisions the Adjustable Interest Rate (LIBOR) Act. The LIBOR Act is largely unchanged from the legislation passed by the U.S. House of Representatives in December 2021, which the U.S. Senate also passed earlier this month as part its approval of The Consolidated Appropriations Act. Some of the highlights:

- As discussed in a previous post on the House bill, the LIBOR Act is intended to provide a transition from LIBOR to a SOFR based rate for "tough" legacy contracts which lack adequate fallback provisions and would be difficult to amend.
- The LIBOR Act does not affect contracts which already contain benchmark replacement or alternate interest rate provisions, so the work in the business loan market (which typically contain some version of fallback language even in credit documents that pre-date LIBOR sunset announcements) will need to continue apace.
- The LIBOR Act also amends the Trust Indenture Act of 1939 to resolve potential conflicts between the provisions of that legislation and changes authorized under the LIBOR Act.
- The Board of Governors of the Federal Reserve System (the Fed) is charged with adopting regulations to implement the LIBOR Act and establish a replacement rate based on SOFR (including establishing spread adjustments for the one, three and six month interest period tenors).
- Perhaps most importantly, the LIBOR Act establishes safe harbor from claims and liability for administrators, trustees or agents which utilize Fed selected benchmark replacements and procedures.

The LIBOR Act will provide important relief for CLOs, bonds and similar widely held and difficult to amend debt instruments, and protection for the trustees and agents which administer those products in dealing with LIBOR transition, but will have little direct impact for the business loan market.

No New LIBOR and its Nuances: As to business loans, throughout the end of Q42021 and early Q12022, we've seen banks methodically implementing the joint OCC and Fed regulatory guidance dictating "no new LIBOR" after December 31, 2021. This has been clearly understood to mean no new LIBOR deals or facility size increases for LIBOR deals after that date, and no extensions of maturity for existing LIBOR deals beyond June 30, 2023 (the final termination date for the publication of LIBOR). The meaning of "no new LIBOR" for other credit actions on and after January 1, 2022 is less clear and much discussed: For instance:

- *Committed delayed draw term loans:* like a committed revolver, probably OK to fund at LIBOR (but probably not OK to extend the draw period)
- *Uncommitted facilities:* some credit facilities are "discretionary", and without an ***obligation*** to lend at LIBOR, the weight of interpretation has settled on – move away from LIBOR absent compelling circumstances
- *Material Credit Actions / Waivers:* some banks have decided to use any material credit action as a basis to move away from LIBOR, e.g., a waiver, forbearance or other action requiring credit committee approval

Regulators have avoided issuing specific bright line guidance on these and other "grey area" questions in an effort to push the market away from LIBOR as quickly as possible – if you're uncertain whether a funding or credit action crosses the "no new LIBOR" line, ask your examiner, with a preference for moving off LIBOR wherever possible.

Term SOFR Adoption: An open question early in Q42021 was whether CME Term SOFR would be widely adopted. That questions has been clearly answered "yes", and CME Term SOFR (now expanded to offer twelve month tenors, along with the original one, three and six month tenors), has become commonplace in syndicated loan transactions. Lower middle market bilateral lending transactions have been showing a variety of alternative approaches, including SOFR varieties (e.g., one month SOFR resetting monthly), BSBY, Ameribor and in some cases, "Prime minus" formulations. ARRC and LSTA model SOFR language has been widely adopted particularly in syndicated transactions, with some negotiation around a few topics:

- *Spread Adjustments:* As previously noted, LIBOR-to-SOFR fallback language recommended by ARRC and industry groups (e.g. the LSTA) included a "spread adjustment" to approximate LIBOR values in a SOFR-based rate calculation, i.e., Term SOFR + Spread Adjustment + Applicable Margin, and on March 5, 2021, the ARRC published recommended spread adjustments for one, three and six month tenors based on the average spread between SOFR and LIBOR during the 5 year period leading up to that date. However throughout 2021 Q2 – Q4, the spread between the SOFR and LIBOR spot rates was lower than the 5 year average, leading to frequent negotiation around those spread adjustment values. That dynamic turned around in 2022 Q1, with international and market turmoil driving LIBOR up (recall LIBOR is more sensitive to credit market shocks than SOFR), and pushing the spot spreads back up to, or even slightly above, the ARRC recommended SOFR spreads.
- *Beyond Spread Adjustments:* While spread adjustments made sense for fallback language designed to kick in at a future "Benchmark Replacement Date", a two part calculation (Term SORF + Applicable Margin, with any additional credit risk built into the Applicable Margin) seems like the better approach for new day-one Term SOFR loans. That approach hasn't yet been widely adopted in our experience, and the "Adjusted Term SOFR" three-part construct described above (with the attendant fluid negotiations around the proper spread adjustment) has become something of the norm, at least through February 2022. However we have seen some movement recently toward the simpler two part construct as lenders have become more comfortable with how to price SOFR based loans.
- *Most Favored LIBOR Transition:* We've seen borrowers occasionally ask for, and lenders occasionally agree to, most favored nation treatment on benchmark replacement setting.
- *Break Funding:* We've seen borrowers regularly ask to remove break funding make-whole language on the theory that SOFR loans are not match-funded, so that there should never be any break funding exposure for lenders. There continues to be debate in the market around the practical utility and application of such provisions, but we have generally seen them retained in credit agreements.

Remediation of Existing LIBOR Contracts: While the market evolves around new day-1 SOFR transactions, lenders are actively working to remediate their shrinking, but still very significant, back-book of LIBOR linked business loans. Although new syndicated debt linked to SOFR outpaced LIBOR in January and February, the total outstanding value of debt products linked to LIBOR is still significant, so with only 5 quarters until the last day of LIBOR publication, much remediation work remains.

By Donald A. Ensing, Susan Rodriguez, James Gelman & Kent Walker on March 31, 2022

McGuireWoods, LLP

When Are CCOs on the Hook? FINRA Offers Guidance on CCO Liability - Latham & Watkins

Guidance clarifies assessment of liability under Rule 3110, including designation as supervisor, application of reasonableness standard, and factors for and against charging compliance officials.

On March 17, 2022, the Financial Industry Regulatory Authority, Inc. (FINRA) published Regulatory Notice 22-10 (Reg. Notice 22-10), reminding broker-dealers of the scope of liability for chief compliance officers (CCOs) under FINRA's Supervision Rule (Rule 3110). The role of compliance, and that of the CCO in particular, which is often characterized as "vital" in helping to prevent, detect, and remediate potential violations of internal policies and procedures and the securities laws, has been the subject of policy debate for some time.[1] In Reg. Notice 22-10, FINRA outlines a blueprint to assess the potential liability of CCOs under Rule 3110.

Rule 3110 imposes various supervisory obligations on member firms, such as the obligation to "establish and maintain a system, including written procedures, to supervise the activities of each associated person that is reasonably designed to achieve compliance with applicable securities laws and regulations, and with applicable FINRA rules." Firms are also required to designate registered principals as supervisors for these responsibilities. The express or implied designation of supervisory authority is the basis for individual liability under Rule 3110.

Assessing Supervisory Responsibility

FINRA clarifies a CCO will be subject to liability under Rule 3110 only when the firm designates the CCO as having supervisory responsibility. The starting point of the analysis is not the title[2] but the designation of supervisory responsibility. The ultimate responsibility for a broker-dealer's compliance rests with its chief executive officer and senior management, not compliance officials.[3]

A CCO can be "designated" as having supervisory responsibility via express designation or, the firm's CEO or other senior business manager can "expressly or impliedly designate the CCO as having specific supervisory responsibilities on an ad hoc basis."

Per Reg. Notice 22-10, CCOs can be "designated" as having supervisory responsibility in the following ways:

1. **Written CCO Supervisory Designation to Establish, Maintain, and Update WSP:** The broker-dealer's written procedures might assign to the CCO the responsibility to establish, maintain, and update written supervisory procedures (WSPs), both generally and in specific areas (e.g., electronic communications).
2. **Written CCO Supervisory Designation to Enforce WSP:** The broker-dealer's written procedures might assign to the CCO the responsibility for enforcing the broker-dealer's WSPs or other specific oversight duties usually reserved for line supervisors.
3. **Ad Hoc Express or Implied CCO Supervisory Designation:** The broker-dealer's president or other senior business manager might also expressly or impliedly designate the CCO as having specific supervisory responsibilities on an ad hoc basis.
4. **CCO Supervisory Designation as Exigencies Demand:** The CCO may be asked to take on specific supervisory responsibilities as exigencies demand, such as the review of trading activity in customer accounts or oversight of associated persons.

FINRA clarifies in Reg. Notice 22-10: “Only in circumstances when a firm has expressly or impliedly designated its CCO as having supervisory responsibility will FINRA bring an enforcement action against a CCO for supervisory deficiencies.”

The Reasonableness Standard

CCOs are not subject to strict liability. Even when a CCO has been designated as having supervisory responsibilities, FINRA would seek to discipline a CCO under Rule 3110 if the CCO failed to discharge those designated supervisory responsibilities in a reasonable manner. The determination of reasonableness in a CCO’s performance of these supervisory responsibilities depends upon the facts and circumstances of each particular situation. FINRA will assess reasonableness in terms of whether the CCO’s conduct was tailored toward achieving compliance with the federal securities laws, regulations, or FINRA rules.

Factors for and Against Charging a CCO under Rule 3110

In assessing potential liability under Rule 3110, FINRA weighs the facts and circumstances of each case to determine whether the CCO’s conduct in performing designated supervisory responsibilities was reasonable in terms of achieving compliance with the federal securities laws, regulations, or FINRA rules.

Not every violation under Rule 3110 results in formal disciplinary charges. FINRA weighs various aggravating and mitigating factors to determine, based on the facts and circumstances of each particular case, whether to bring formal or informal disciplinary action (e.g., a Cautionary Action Letter).

Aggravating factors include awareness of multiple red flags or actual misconduct and failure to take steps to address them, as well as failure to establish, maintain, update, or enforce a firm’s WSPs. FINRA would also assess whether the CCO’s supervisory failure resulted in violative conduct, and whether that conduct caused or created a high likelihood of customer harm.

Mitigating factors include whether the CCO was given insufficient staffing, budget, and training; whether the CCO was unduly burdened in light of competing functions and responsibilities; whether the supervisory responsibilities were poorly defined or designated; whether the firm underwent structural changes; and whether the CCO attempted to escalate such red flags to firm leadership in a good-faith effort to reasonably discharge supervisory responsibilities.

The SEC Standard for CCO Liability

Rule 3110 differs in some key respects from the application of Rule 206(4)-7 (Compliance Rule) under the Advisers Act, or Section 15(b) of the Securities Exchange Act of 1934.

Under the Compliance Rule, an investment adviser subject to SEC jurisdiction must adopt and implement written policies and procedures reasonably designed to prevent violation of the Investment Advisers Act of 1940 (Advisers Act) by the investment adviser or any of its supervised persons. The CCO must be designated to administer these policies and procedures and should also have sufficient seniority and authority within the organization to compel others in the organization to adhere to the compliance policies and procedures.

Under Section 15(b)(6) of the Securities Exchange Act of 1934, the SEC may take action against an individual associated with a broker-dealer if someone under that person’s supervision violated the federal securities laws, the Commodity Exchange Act, the rules or regulations under those statutes, or the rules of the Municipal Securities Rulemaking Board; and the individual failed reasonably to

supervise that person to prevent the particular violation.

The issue was central to *In the Matter of Theodore W. Urban*, an administrative proceeding decided on September 8, 2010. The order in the proceeding relied on an earlier proceeding decided in December 1992 (*In the Matter of John H. Gutfreund, et. al.*), which noted that, "[D]etermining if a particular person is a "supervisor" depends on whether, under the facts and circumstances of a particular case, that person has a requisite degree of responsibility, ability or authority to affect the conduct of the employee whose behavior is at issue." (emphasis added).

On September 30, 2013, the SEC's Division of Trading and Markets published a set of eight Frequently Asked Questions (FAQs) concerning supervisory liability for compliance and legal personnel at broker-dealers under Sections 15(b)(4) and 15(b)(6) of the Exchange Act. These FAQs stated that the Urban decision was considered "of no effect" (and therefore not adverse precedent). Liability under Section 15(b) continues to be a facts-and-circumstances determination regarding "the requisite degree of responsibility, ability or authority to affect the conduct of the employee whose behavior is at issue." SEC staff clarify, in the FAQs, that certain facts on their own are not sufficient to turn legal or compliance personnel into supervisors. These facts include:

- Holding a compliance or legal position
- Providing advice or counsel concerning compliance or legal issues to business line personnel or even senior management
- Assisting in the remediation of an issue
- Participating in, providing advice to, or consulting with a management or other committee

For the SEC, the real question is not necessarily whether a CCO has been explicitly or implicitly designated a supervisor, but whether the person clearly has been given, or otherwise assumed, the requisite degree of responsibility, ability, or authority to affect the conduct of another employee.

In a November 4, 2015 speech, Andrew Ceresney, then-Director of the Division of Enforcement, further outlined the SEC's "longstanding careful and measured approach" to liability for CCOs of investment advisers, but also to broker-dealers and dual registrants. He noted that "after a thorough analysis of the facts and circumstances and consideration of fairness and equity," the SEC has charged CCOs primarily when the CCO directly participated in misconduct unrelated to compliance duties, such as fraud; obstructed or misled SEC Staff; or has exhibited wholesale failures in carrying out clearly assigned responsibilities, such as developing and implementing WSPs.

In one notable case that he described, a large money manager did not have any written policies and procedures regarding the outside business activities of its employees. Despite awareness of this gap and numerous red flags among employees, "the CCO failed to develop and implement written policies and procedures to assess and monitor the outside activities of the firm's employees and to disclose related conflicts of interest to the funds' boards and to advisory clients." The CCO, however, was not charged with failure to disclose the conflicts of interest; he was charged with failure to adopt written policies regarding outside business activities.

While the SEC's standard remains a fact-intensive inquiry, the SEC clearly does not consider a CCO's provision of counsel to the business (whether effective or ineffective) as grounds for supervisory liability without further analysis of the CCO's degree of responsibility, ability, or authority.

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[1] See, e.g., Securities and Exchange Commission, Commissioner Luis A. Aguilar, The Role of Chief

Compliance Officers Must be Supported (June 29, 2015), available at https://www.sec.gov/news/statement/supporting-role-of-chief-compliance-officers.html.

[2] According to FINRA, "The CCO's role, in and of itself, is advisory, not supervisory." Reg. Notice 22-10; Likewise, SEC staff has noted, "Compliance and legal personnel are not 'supervisors' of business line personnel for purposes of Exchange Act Sections 15(b)(4) and 15(b)(6) solely because they occupy compliance or legal positions." Securities and Exchange Commission, Division of Trading and Markets, Frequently Asked Questions about Liability of Compliance and Legal Personnel at Broker-Dealers under Sections 15(b)(4) and 15(b)(6) of the Exchange Act, at question 1 (Sept. 30, 2013), available at https://www.sec.gov/divisions/marketreg/faq-cco-supervisi-n-093013.htm; According to a statement by Jessica Hopper, FINRA Head of Enforcement, a CCO's role within a firm does not "automatically make them supervisors" subject to the requirements under Rule 3110.

[3] Id. at Background and fn 4, citing to Sheldon v. SEC, 45 F.3d 1515, 1517 (11th Cir. 1995); FINRA Regulatory Notice 22-10 ("The responsibility to meet these obligations rests with a firm's business management, not its compliance officials.").

Latham & Watkins LLP – Marlon Q. Paz, John J. Sikora Jr., Stephen P. Wink and Deric M. Behar

March 31 2022

Reminder: SEC Requires Disclosure of Rating Changes and Financial Obligations - Dinsmore & Shohl

When it comes to continuing disclosure, two of the more common "material events" to occur are rating changes and the incurrence of a "financial obligation." As a general matter, these are reportable events that should be posted to Electronic Municipal Market Access (EMMA). However, as a practical matter, these material events are frequently overlooked.

Whether a rating change involves an upgrade or a downgrade, it is necessary to post such changes to EMMA pursuant to SEC Rule 15c2-12 (the SEC Rule) for those issuers who are subject to the SEC Rule, even though municipal ratings are usually considered public knowledge. Typically, a change in outlook (such as stable, positive, or negative) is not considered a rating change for the purpose of the SEC Rule, although there is no prohibition in voluntarily posting a notice of such a change on EMMA.

On March 18, 2022, Moody's Investors Service upgraded the "insurance financial strength" rating of bond insurer Assured Guaranty Municipal Corp. (AGM) and Assured Guaranty UK Limited (AGUK) to A1 from A2. A number of holding companies of Assured Guaranty were also upgraded. For those issuers, and other obligated persons, having issued bonds or other municipal obligations utilizing the credit of Assured Guaranty in the form of bond insurance or other credit enhancement, and who

have continuing disclosure responsibilities under the SEC Rule, consideration should be given to disclosing this upgrade.

In the absence of an exception, the SEC Rule mandates underwriters of municipal securities ensure issuers or other obligated persons undertake to provide to the public continuing disclosure information presumed to be important to investors by filing that information with EMMA. Among other things, the SEC Rule requires issuers or obligated persons who have agreed to a continuing disclosure undertaking must provide the MSRB notice of: (a) payment delinquencies and defaults; (b) unscheduled draws on debt service reserves or credit enhancements; (c) substitution of credit or liquidity providers; (d) adverse opinions or notices from the Internal Revenue Service (IRS); (e) bond calls or tender offers; (f) defeasances; (g) bankruptcy; (h) ratings changes; and (i) a default, event of acceleration, termination event, modification of terms or similar event. Although there are other material events, those material events are qualified by a "materiality" standard, such as the disclosure of the incurrence of "financial obligations." Any issuer or obligated person who has agreed to a continuing disclosure undertaking must notify the MSRB of the forgoing events within 10 business days.

Dinsmore & Shohl LLP – Bradley N. Ruwe and Joshua D. Grossman

March 25 2022

Hawkins Advisory: The Federal Adjustable Interest Rate (LIBOR) Act

The attached Hawkins Advisory discusses recent federal legislation that addresses a variety of legal issues arising from the anticipated June 30, 2023 phase-out of the use of United States dollar denominated LIBOR.

Read the Hawkins Advisory.

President Biden Signs Bill Expanding Cybersecurity Reporting Obligations.

President Biden signed the Consolidated Appropriations Act, 2022 into law on March 15, 2022. Section Y of the new omnibus appropriations bill is titled The Cyber Incident Reporting for Critical Infrastructure Act of 2022 ("the Act"). Importantly, the Act significantly expands federal cybersecurity incident and ransom demand reporting requirements for critical infrastructure entities. In light of these new requirements, critical infrastructure entities who suspect that they may be subject to the Act should begin investigating how the Act will impact their business and consider establishing protocols which may be necessary to ensure compliance.

Notably, the Act does not directly define many necessary terms and obligations. Instead, the Department of Homeland Security's Director of the Cybersecurity and Infrastructure Security Agency ("CISA") has been tasked with promulgating a final rule finalizing these definitions and obligations. Within 24 months of the Act's enactment, CISA is required to begin the notice-an--comment rulemaking process. The final rule must then be published within the 18 months following the start of the rulemaking process. Interested stakeholders will want to review the proposed rule promptly when it is released and consider submitting comments as appropriate.

Incident Reporting Obligations

With respect to incident reporting, the Act requires covered entities to comply with new and expanded obligations when they experience a "covered cyber incident." The term "covered entity" means a critical infrastructure entity—as defined by Presidential Policy Directive 21 ("the Directive")—that satisfies the criteria established in CISA's final rule. Although CISA's criteria will remain unknown until the final rule is promulgated, the Directive clarifies the types of entities that may be subject to the expanded requirements.

Under the Directive, critical infrastructure entities are those operating in the following sectors:

- **Chemical sector.** Including manufacturing, storing, using, or transporting potentially dangerous chemicals.
- **Commercial facilities sector.** Includes a range of sites that are open to the public and draw large crowds for shopping, business, entertainment or lodging.
- **Communications sector.** Includes satellite, wireless and wireline providers, which depend on each other to carry and terminate their traffic.
- **Critical manufacturing sector.** Encompasses the production of primary metals; machinery; electrical equipment, appliances and components; and transportation equipment that may be susceptible to man-made and natural disasters.
- **Dams sector.** Delivers water retention and control services in the United States, including hydroelectric power generation, municipal and industrial water supplies, agricultural irrigation, sediment and flood control, river navigation for inland bulk shipping, industrial waste management and recreation.
- **Defense industrial base sector.** Encompasses research and development, as well as the design, production, delivery and maintenance of military weapons systems, subsystems and components to meet U.S. military requirements. The sector provides products and services for mobilizing, deploying and sustaining military operations. It does not include the commercial infrastructure of those who provide services such as power, communications, transportation or utilities, which are covered under other sectors.
- **Emergency services sector.** Includes law enforcement, fire and rescue services, emergency medical services, emergency management and public works.
- **Energy sector.** Includes entities that focus on electricity, oil and natural gas.
- **Financial services sector.** Includes depository institutions, providers of investment products, insurance companies, and other credit and financing organizations, as well as the providers of the critical financial utilities and services that support these functions.
- **Food and agriculture sector.** Includes farms, restaurants, and registered food manufacturing, processing and storage facilities.
- **Government facilities sector.** Includes general-use office buildings and special-use military installations, embassies, courthouses, national laboratories and structures.
- **Healthcare and public health sector.** Focuses on protecting all sectors of the economy from terrorism, infectious disease outbreaks and natural disasters.
- **IT sector.** Covers hardware, software, and IT systems and services, along with the communications sector and the internet.
- **Nuclear reactors, materials and waste sector.** Encompasses most aspects of America's civilian nuclear infrastructure, such as nuclear facilities, materials and waste, as well as any cybersecurity related to these facilities.
- **Transportation systems sector.** Focuses on safely, securely and efficiently moving people and goods through the country and overseas. Subsectors include aviation, highway and motor carrier, maritime transport system, mass transit and passenger rail, pipeline systems, freight rail, postal and shipping.

- **Water and wastewater systems sector.** Concentrates on ensuring the supply of drinking water and wastewater treatment.

Similar to the definition of "covered entity," the full definition of "covered cyber incident" will not be available until CISA publishes the final rule. However, the Act establishes that the definition of "covered cyber incident" will contain certain key elements. Pursuant to the Act, the final rule's definition of "covered cyber incident" must require, at minimum, the occurrence of:

- A cyber incident that leads to substantial loss of confidentiality, integrity or availability of such information system or network, or a serious impact on the safety and resiliency of operational systems and processes;
- A disruption of business or industrial operations, including due to a denial of service attack, ransomware attack or exploitation of a zero-day vulnerability against 1) an information system or network, or 2) an operational technology system or process; or
- Unauthorized access or disruption of business or industrial operations due to loss of service facilitated through, or caused by, a compromise of a cloud service provider, managed service provider or other third-party data hosting provider, or by a supply chain compromise.

CISA's final rule will also outline many substantive requirements such as incident reporting obligations and ransom reporting obligations. In each instance, the final rule shall require a covered entity to report the following within 72 hours of the covered entity's reasonable belief that a covered cyber incident has occurred:

- A description of the "covered cyber incident including i) identification and a description of the function of the affected information systems, networks, or devices that were, or are reasonably believed to have been, affected by such cyber incident, ii) a description of the unauthorized access with substantial loss of confidentiality, integrity, or availability of the affected information system or network or disruption of business or industrial operations, iii) the estimated data range of such incident, and iv) the impact to the operations of the covered entity;"
- A description of the vulnerabilities exploited and the security defenses that were in place, as well as the tactics, techniques, and procedures used to perpetrate the "covered cyber incident;"
- Any identifying or contact information related to each actor reasonably believed to be responsible for such cyber incident;
- The category or categories of information that were, or are reasonably believed to have been, subject to unauthorized access or acquisition;
- Identification information of the impacted entity; and
- Contact information for the impacted entity or an authorized agent of the entity.

In the event that a covered entity makes a ransom payment, the final rule will also require the covered entity to make the following disclosures to CISA within 24 hours of such payment:

- A description of the ransomware attack, including the estimated date range of the attack;
- A description of the vulnerabilities, tactics, techniques, and procedures used to perpetrate the ransomware attack;
- Any identifying or contact information related to the actor or actors reasonably believed to be responsible for the ransomware attack;
- The name and other information that clearly identifies the covered entity that made the ransom payment or on whose behalf the payment was made;
- The contact information of the covered entity or authorized agent that made the ransom payment;
- The date of the ransom payment;
  The ransom payment demand, including the type of virtual currency or other commodity requested;
- The ransom payment instructions; and

- The amount of the ransom payment.

Additionally, the Act also requires a covered entity to submit updated reports to supplement previously provided information when substantial new information is discovered. Once a report is submitted, all data relevant to the "covered cyber incident" or ransom payment must then be preserved by the covered entity pursuant to procedures yet to be established through the rulemaking process.

Exceptions to Reporting Obligations

The exceptions to these reporting obligations are fairly narrow. For instance, while a covered entity would otherwise be required to make two reports to cover both a covered cyber incident and a ransom payment, the Act allows such an entity to combine all required information into a single report. Similarly, in the event that a covered entity is subject to certain reporting requirements to other Federal agencies, the report to the other agency may satisfy the entity's reporting obligations to CISA provided that a sharing agreement between the agencies exists.

Using a Third Party to Submit a Required Report or Make a Ransom Payment

A covered entity may either submit a required report itself or use a third party to do so. Such a third party can include an entity such as an "incident report company, insurance provider, service provider, Information Sharing and Analysis organization, or law firm." In the event that a covered entity utilizes a third party, it must be aware that the use of such a third party does not relieve the covered entity from its reporting requirement. Rather, a covered entity utilizing a third party is subject to the same reporting obligations and timelines as it would be had it submitted the report or made the ransom payment itself.

Notably, third parties are largely exempt from independent obligations under the Act. Importantly, where a third party submits a report or makes a ransom payment on behalf of a covered entity, that third party is not obligated to submit a separate report on its own behalf. However, such a third party does have an obligation to advise the covered entity of their responsibilities regarding the covered entity's reporting obligations. Thus, businesses who act as third parties and provide reporting services to covered entities should remain apprised of all reporting requirements and prepare to advise their clients.

Incident Report Sharing and Data Use

Though the Act establishes substantial reporting obligations, it also limits CISA's ability to use and share the information provided by covered entities in the reports. Importantly, such information may only be used by the Federal Government for:

- Cybersecurity purposes;
- Identifying a cyber threat or security vulnerability;
- Purposes of responding to, "or otherwise preventing or mitigating, a specific threat of death, a specific threat of serious bodily harm, or a specific threat of serious economic harm;"
- Purposes of "responding to, investigating, prosecuting, or otherwise preventing or mitigating, a serious threat to a minor;" or
- Purposes of "preventing, investigating, disrupting, or prosecuting an offense arising out of a reported cyber incident."

In addition to the limitations on use, similar to other cyber threat information-sharing opportunities provided by the Federal Government, information contained in required reports is afforded further

protections. Importantly, information obtained by CISA via a required report may not act as the basis for any cause of action. Similarly, such information is also protected from admission into evidence in any future proceeding. Thus, any information contained in a required report may not be received into evidence, subjected "to discovery, or otherwise used in any trial, hearing, or other proceeding in or before any court, regulatory body, or other proceeding."

In providing these protections, the Act intends to enable covered entities to fully disclose all relevant information regarding a covered cyber incident without incurring the risk of potentially exposing itself to liability due to the content of the report. Additional protections establish that information disclosed to CISA pursuant to the Act:

- Is considered to be the "commercial, financial, and proprietary information of the covered entity when so designated by the covered entity;
- Is exempt from disclosure under the Freedom of Information Act (FOIA);
- Is exempt from disclosure required by any "State, Tribal, or local freedom of information law;"
- Is not considered to be a waiver of any "applicable privilege or protection provided by law, including trade secret protection;" and
- May be shared externally only when the victim's identity is anonymized.

Enforcement

In the event that a covered entity fails to comply with the new cyber incident reporting obligations, CISA's director may request information if it suspects the entity of noncompliance. If the covered entity fails to respond within 72 hours, CISA may then issue an administrative subpoena. Should the covered entity subsequently fail to comply with the subpoena, CISA may turn the matter over to the U.S. Attorney General for civil enforcement and covered entity may potentially held in contempt of court.

However, prior to exercising their enforcement authority, the CISA director must first consider i) the complexity of determining whether a covered cyber event has occurred as well as ii) the covered entity's previous interactions with the agency and the likelihood that the entity is aware of its reporting obligations.

Other Notable Provisions

In addition to expanding reporting obligations, the Act also creates several entities and programs intended to improve the state of cybersecurity in the U.S. These additional provisions call for the creation of:

- The Cyber Incident Reporting Council, led by the Secretary of Homeland Security, which will be responsible for coordinating, deconflicting, and harmonizing Federal incident reporting requirements;
- A ransomware vulnerability warning pilot program intended to "leverage existing authorities and technology to specifically develop processes and procedures for . . . identifying information systems that contain security vulnerabilities associated with common ransomware attacks, and to notify the owners of those vulnerable systems of their security vulnerability;" and
- The "Joint Ransomware Task Force to coordinate an ongoing national campaign against ransomware attacks, and identify and pursue opportunities for international cooperation."

Key Takeaways

Though there is much that will remain unclear until CISA promulgates the final rule, businesses

should, at the very least, be aware of the following:

To whom does the Act apply? The Act applies to covered entities as defined by CISA.

What does the act mandate? Reports must be made to CISA when the covered entity makes a ransom payment or experiences a covered cyber incident.

When must the report be made? Reports must be made to CISA within 72 hours of a business's reasonable belief that a covered cyber incident has occurred and 24 hours of any ransom payment.

How is the information contained in the reports protected? CISA may only use the information in the reports for very limited purposes outlined above. Such information is further protected from disclosure via discovery, FOIA requests, or other open records requirement, etc.

How is the Act enforced? The CISA may request information in the event that it believes a covered entity may be noncompliant. If the entity fails to respond to the request within 72 hours, the CISA may issue a subpoena. If the entity fails to respond to the subpoena, the CISA may turn the matter over to the U.S. Attorney General who may enforce the subpoena.

Crowell & Moring LLP – Sarah Rippy, Matthew B. Welling, Evan D. Wolff, Maida Oringher Lerner, Alexander Urbelis and Michael G. Gruden

March 24 2022

SEC Settles Municipal Bond Fraud Case Against Texas School District and Former CFO, and Suspends External Auditor.

On March 16, the SEC filed a municipal bond fraud case against Crosby Independent School District and its former CFO in a $20 million bond offering.1 Crosby is a suburb of Houston, Texas. The SEC also charged the district's outside auditor with improper professional conduct and suspended her from appearing or practicing before the Commission with a right to reapply after three years.

A review of the allegations reveals that the case involved classic financial reporting fraud. The SEC alleged that Crosby ISD's year-end 2017 financial statements seriously understated its payroll and construction liabilities by failing to report some $11.7 million of such liabilities. Those same audited financial statements also contained false claims that the district had $5.4 million in general fund reserves, thereby substantially overstating its assets. According to the Commission, the district and the then-CFO knew that the financial statements were false but issued them anyway. The CFO also allegedly signed false management representation letters. The false statements also appeared in the offering documents for the municipal bond sale.

The fraud allegedly came to light in June 2018 when the successor CFO discovered the misstatements. In August 2018, seven months after the offering, the district disclosed significant financial distress, including that it had a negative general fund balance. The following month, ratings agencies downgraded the district's bonds.

The audit partner agreed to a suspension from appearing or practicing before the Commission under Rule 102(e) of the Commission's Rules of Practice.2 The Commission charged her with improper professional conduct, including failure to obtain sufficient audit evidence, improper supervision of the audit, and lapses in professional judgment and professional skepticism.

The settlements with the district and the former CFO, which were made on a neither-admit-nor-deny basis, involve alleged violations of the antifraud provisions of the federal securities laws, including Exchange Act Section 10(b) and Exchange Act Rule 10b-5.3 The former CFO agreed to pay a $30,000 penalty and not participate in any future municipal securities offerings.

The case is a reminder that the SEC is the cop on the beat in municipal securities offerings and will enforce the securities laws when violations occur.

Footnotes

1. SEC Press Release, *SEC Charges Texas School District and its Former CFO with Fraud in $20 Million Bond Sale* (Mar. 16, 2022), available here.

2. Order Instituting Public Administrative Proceedings Pursuant to Section 4C of the Securities Exchange Act of 1934 and Rule 102(e) of the Commission's Rules of Practice, Making Findings, and Imposing Remedial Sanctions, Securities Exchange Act Release No. 94426 (Mar. 16, 2022), available here.

3. Order Instituting Cease-and-Desist Proceedings Pursuant to Section 8A of the Securities Act of 1933 and Section 21C of the Securities Exchange Act of 1934, Making Findings, and Imposing A Cease-and-Desist Order, Securities Act Release No. 11039 (Mar. 16, 2022), available here.

by Toby M. Galloway

23 March 2022

Winstead PC

The Curious Story of How CUSIP Numbers Became a Wall Street Battleground.

CUSIP numbers are like a Dewey Decimal System for stocks and bonds. They're also a source of illegal monopoly power, according to investor lawsuits.

They may not be the most exciting part of the securities markets, but CUSIP numbers are indispensable.

The arcane nine-digit ID numbers, issued by the Committee on Uniform Securities Identification Procedures, show up on everything from stocks, bonds, exchange-traded securities and mutual funds. They're also not free. In at least two class-action lawsuits, investors are alleging that the cost of CUSIPs has been artificially inflated for decades, as a result of monopolistic control by data providers including the American Bankers Association, FactSet and S&P Global.

Investors, who are seeking injunctions and damages, allege the CUSIP system's owners and exclusive licensees aggressively sought to dampen competition from other services offering free or lower-cost alternatives.

"The motive for their exclusion of competition is simple," says one of the complaints filed recently in

Manhattan federal court, “CUSIPs are worthless except for the fact that they are the standard.”

How the CUSIP system began

CUSIPs have been standard since the 1960s for identifying securities for clearing and settlement of trades. The system is owned by the ABA and a subsidiary of S&P’s Global Market Intelligence, now called Factset Research Systems, which completed its purchase of the business from S&P this month for $1.925 billion.

The numbering system was originally a subscription service that provided physical books containing information on every financial instrument linked to a CUSIP and were updated quarterly or annually. But in the 1980s, vendors like Bloomberg began distributing the data directly and electronically to financial institutions, making it unnecessary to pay a fee to S&P.

To counter the loss of revenue, S&P changed its business model from a subscription service to a licensing one, and required financial firms using CUSIPs to pay substantial fees. S&P inserted language in its contracts with data vendors requiring them to cut off access to the CUSIPs for any financial institution that did not enter into a license agreement with S&P.

At about the same time, according to the lawsuits, ABA and S&P became more aggressive in trying to maintain their stranglehold on the system.

“Monopolies are rarely good for business,” said Ronald J. Aranoff, a partner in the Litigation & Dispute Resolution Group at Wollmuth Maher & Deutsch LLC, which represents plaintiff Hildene Capital Management. “We trust the court to decide whether the exercise of monopoly power here was unlawful. We believe it is.”

Flexing monopoly power

CUSIP was designated as a financial standard by a committee of the American National Standards Institute (ANSI), dubbed X9. But X9 is hardly an independent body, at least according to the class action suits. The ABA established X9 during the 1970s and it, as well as S&P’s CUSIP Global Services, are still connected to X9 through voting positions on the committee’s board of directors.

Hildene is an institutional asset manager headquartered in Stamford, Conn. Like all other investment managers and traders, it requires access to financial information for managing, monitoring, buying, and selling financial instruments. The company typically pays Bloomberg for access to data that includes CUSIP numbers. For Hildene, the cost of getting the data with CUSIP numbers ends up being about $10,500 a year.

“Hildene…[is] then left with two unenviable options: pay S&P’s supracompetitive subscription rates or have CUSIP numbers stripped from their data feed and suffer, at a minimum, significant disruption to their businesses,” the lawsuit states.

Hildene once balked at paying the licensing fees, and was sent “a series of increasingly hostile letters” and threats that it must pay the fee or face a debilitating lock out from access to CUSIP numbers, according to the suit. With no alternative, Hildene eventually signed the subscription agreement.

Making money by owning CUSIPs

The CUSIP owners generate revenue in at least three ways. First, S&P, now Factset, charges securities issuers a fee, typically about $280 per CUSIP number, to obtain CUSIP numbers for its

securities. Second, S&P charges data providers, like Bloomberg, licensing fees for using CUSIPs in its databases. Third, and more recently, S&P demands that end users, like Hildene, enter their own subscription agreements with S&P under the threat of having the numbers stripped from their data feeds.

“Defendants have a clear interest in requiring that all data users use only the CUSIP identifier system,” according to the suit. “That is because…the ABA retains 30% of CGS’s licensing fees from all data users and the remainder is kept by S&P.”

An earlier class-action complaint by Dinosaur Financial Group LLC further alleges that ABA and S&P are violating copyright laws, on the premise that ID numbers like CUSIP numbers can’t be protected by copyrights.

“A CUSIP is a number that has been known to humanity literally for millennia,” the complaint says. “ Mathematicians, scientists, teachers, and financial markets’ participants use numbers every day that happen to coincide with CUSIP numbers. Yet, defendants assert that the ABA has copyrighted those numbers and therefore can control the use of those numbers. That assertion is legally baseless.”

Attempts to reach the ABA and S&P for comment about the suits were unsuccessful.

Past antitrust complaints

Complaints about the CUSIP system and allegations that it unfairly restrains competition have surfaced multiple times throughout its history.

In November 2009, the European Commission accused S&P of abusing its position as the sole provider of ISIN codes – the international version of the CUSIP – by requiring European financial firms and data vendors to pay licensing fees for their use. The European Commission noted that there are no acceptable alternatives for traders and financial institutions.

Although it disagreed with the commission’s findings, S&P offered to create a lower-cost alternative feed of certain ISINs for market participants in Europe.

The Center for Municipal Finance, a U.S.-based nonprofit dedicated to improving the municipal bond market, has come out in support of a free alternative to CUSIPs, developed by Bloomberg, called Financial Instrument Global Identifiers. It’s unclear however, whether the FIGI will gain traction in the market because it is not recognized as an industry standard.

“CUSIP is not the United States’ financial instruments identifier standard because of any special technology or knowledge by S&P or ABA,” Hildene said in its complaint. “After all, a CUSIP is just a string of numbers and letters. S&P is not uniquely capable of issuing and maintaining alphanumeric strings.”

businessofbusiness.com

by Doug Bailey

3.25.22

MSRB Fair Dealing Solicitor Municipal Advisor Obligations and New Draft Rule G-46: SIFMA Comment Letter

SUMMARY

SIFMA provided comments to the Municipal Securities Rulemaking Board (MSRB) on their Notice (MSRB Notice 2021-18) on fair dealing solicitor municipal advisor obligations and new draft Rule G-46.

View the MSRB Comment Letter.

March 15, 2022

Groups Raise Concern about Recordkeeping in MSRB Draft Rule.

Comments on the Municipal Securities Rulemaking Board's second request for comment on its draft solicitor muni advisor rule highlight concerns over recordkeeping expectations, harmonization with the Securities and Exchange Commission's "Pay-to Play" rule and whether oral or written disclosures are the most effective for municipal advisors.

The board received comments from The Securities Industry and Financial Markets Association, The National Association of Municipal Advisors and The Third Party Marketers Association. The rule would codify interpretive guidance from 2017 on MSRB Rule G-17 and align obligations under MSRB Rule G-42, the duties of non-solicitor MAs. The board had previously floated a draft of the rule about a year ago.

Susan Gaffney, executive director of NAMA, initially called the efforts to improve draft Rule G-46 a step forward but expressed "extreme concern" over the books and records discussion detailed in the board's second proposal.

In its second RFC, the MSRB proposed including recordkeeping expectations int the text of the rule itself, rather than including it in MSRB Rule G-8 on books and records. The board would then take a similar approach with respect to future MSRB rules or rule amendments with the goal of including books and records obligations to each MSRB rule in the text of each rule itself.

"Finding a proposed change that impacts the entirety of MSRB recordkeeping rules within a rule about solicitors, and without specifically highlighting the larger implications of such a change, is very surprising," the NAMA letter said. "As a matter of principle, proposed broad changes to MSRB rulemaking should not be tucked away in unrelated proposed rulemaking."

NAMA doesn't necessarily disagree that a new rule would be out of place, but wants to emphasize that MSRB rulemaking should be clear and avoid "confusion between inter-and intra- agency rulemakings," the NAMA letter said.

NAMA also supports the MSRB's efforts to have disclosures provided in writing instead of given orally, an issue that the Third Party Marketers Assocation's letter also discussed.

NAMA emphasized the need to not burden small firms with additional requirements, a cause the group stressed to the MSRB many times in recent years.

SIFMA's comment letter applauded the MSRB's efforts in this area but outlined a number of areas where there could be confusion.

"We do, however, still have certain concerns with the (1) lack of solicitation prohibition for solicitor municipal advisors, (2) inconsistency with the SEC's Pay-to-Play Rule (as defined herein), (3) lack of safe harbor for inadvertent solicitation, and (4) recordkeeping requirements," the SIFMA letter said.

The SIFMA letter went on to recommend that Rule G-46 should include a broad solicitation prohibition for solicitor municipal advisors; that the updated rule should include a narrow solicitation prohibition for solicitor municipal advisors if the board doesn't adopt a broad one; alignment with the SEC's Pay-to-Play Rule in addition to a uniform approach for dealers and solicitor municipal advisors.

SIFMA's concerns went deeper to express a lack of safe harbors for inadvertent solicitation, which the group detailed in its original response to the G-46 RFC, concerns around recordkeeping requirements, and a streamlining of future MSRB rules and rule amendments.

"The MSRB stated that it is proposing to take a similar approach with respect to future MSRB rules or rule amendments," the SIFMA letter said. "The MSRB stated that the eventual goal would be to include recordkeeping requirements applicable to each rule in the text of each rule itself instead of Rule G-8."

"We think the overall approach for future MSRB rules and rule amendments is a substantial change to the structure of the MSRB Rulebook and should be open for public comment," the SIFMA letter said.

The Third Party Marketers Association took issue with the "prohibition added to prevent a solicitor municipal advisor from receiving 'excessive compensation' will be problematic," their letter said.

"Although we believe the rationale behind the prohibition to prevent a solicitor municipal advisor from receiving 'excessive compensation' is sound, the determination of what is considered 'excessive compensation' is left open to interpretation," the Third Party Marketers Association letter said. "For non-solicitor municipal advisors and underwriters, the marketplace in which these firms operate is much more robust than the one that exists for solicitor municipal advisors."

By Connor Hussey

BY SOURCEMEDIA | MUNICIPAL | 03/16/22 11:25 AM EDT

ESG Risks for Financial Institutions Operating in the United States: What to Expect in 2022 - Jones Day

In Short

The Background: Demand for ESG-aligned companies and investment products are likely to continue to accelerate transformation of the investing landscape in 2022.

The Issues: Although investor demand for ESG-related transactions continues to grow, these opportunities, along with the markets' and regulators' focus on ESG-related issues, can create significant legal uncertainty and risk for financial institutions. The conflict in Ukraine has only

further complicated these considerations, although the direction and scope of its impact on ESG considerations is very much an open question.

Looking Ahead: The prominence of ESG-related issues in both the financial markets and the public discourse will present opportunities, but also create significant risks, for financial institutions in 2022, which may be magnified in light of the current broader geopolitical context.

ESG considerations will continue to play an ever-increasing role in financial markets in 2022. ESG-related transactions will continue to present significant opportunities for financial institutions as they respond to and support the needs of the market. However, these opportunities, along with the markets' and regulators' focus on other ESG-related issues, can create significant risk. ESG-focused concerns for financial institutions generally arise in two broad contexts: (i) disclosure-related risks and (ii) conduct-related risks.

This Commentary updates our prior observations concerning potential litigation and regulatory risks for financial institutions, including risks posed by governmental and private actors. We will provide additional updates, including as the impacts of the conflict in Ukraine continue to take shape.

Increased Engagement from Regulators

Last year saw frequent engagement by financial regulators focused on ESG issues, including following President Biden's May 2021 Executive Order directing multiple federal agencies to assess climate-finance risks. The Executive Order singled out financial institutions, noting: "The failure of financial institutions to appropriately and adequately account for and measure [climate-related financial risks] threatens the competitiveness of U.S. companies and markets … and the ability of U.S. financial institutions to serve communities."

This trend likely will continue in 2022 with regulators, led in some respects most visibly by the SEC, poised to enact new reporting requirements focused on climate risk and other ESG themes. SEC Chair Gary Gensler has made clear that a new climate risk disclosure rule likely is forthcoming. Reports indicate that a proposed rule could be issued as early as March 21, 2022, and we will provide further updates as appropriate in the coming days. In the meantime, the Climate and ESG Task Force created by the SEC in 2021 continues its work on ESG-related enforcement initiatives, which can proceed even in the absence of any new formal rulemaking process. These developments are of particular significance to financial institutions both in connection with their preparation of disclosures concerning their own corporate activities as well as any disclosures they may be required to make concerning lending or investing activity.

Other financial regulators are similarly expected to place greater emphasis and focus on climate change and broader ESG issues in the coming months. And, in November 2021, the Acting Comptroller of the Currency urged large bank boards to consider five climate change-related questions to "help put into motion the concrete steps that banks need to prudently manage climate risk." The Consumer Financial Protection Bureau has also announced that it will take action focused on racial equity, suggesting that it could even look beyond fair-lending violations in charging unlawful discrimination. Market participants await further announcements from the Department of Labor regarding the October 2021 proposals regarding the extent to which investment manager fiduciaries may consider sustainability factors when assessing investment opportunities.

Although it remains to be seen what the ultimate regulatory framework and reporting requirements for financial institutions will look like and how they will operate in practice, the question of regulatory reporting and disclosures on ESG-alignment is no longer one of "if," as opposed to "when" and "how."

Increased Engagement by NGOs

Financial institutions' ESG-alignment and mitigation of related risks will also likely continue to be a major focal point for non-governmental organizations ("NGOs") and other private stakeholders, including in light of the broader geopolitical context involving the conflict in Ukraine and the increased focus on world energy markets. Financial institutions must balance pressure from NGOs to reduce financing activities of so-called "fossil fuel" companies with the practical reality that such companies outside of Russia will need increased financing to meet the global demand for energy.

In 2021, numerous NGOs scrutinized companies' net-zero commitments and other climate-related statements both inside and outside of the courtroom, and that trend is expected to continue. In December 2021, for instance, the Sierra Club and Center for American Progress jointly issued a report noting that "the U.S. financial sector has not yet responded in a manner that suggests an understanding of either the scale of the crisis or the sector's role in causing it." That report is just one of several issued in 2021 that critically examine the role financial institutions can and should play in climate change. And these efforts are attracting the attention of lawmakers. For example, Representative Katie Porter (CA), teaming up with "Stop the Money Pipeline," a coalition of environmental groups targeting asset managers and banks with net zero pledges, asserted that: "Banks have bankrolled the climate crisis … And they continue to do it today."

NGOs are also actively considering litigation theories or other public pressure tactics against multinational companies in connection with the conflict in Ukraine. For example, the French affiliates of Friends of the Earth and Greenpeace are reported to have sent a letter to a major French energy company requesting it to end business activities connected to the Russian energy market that may "contribute to the commission of serious violations of human rights."

It is likely that financial institutions and large, multinational organizations will continue to be a primary target of NGOs and other activist organizations pursuing traditional litigation proceedings and less-traditional dispute resolution mechanisms to advance their agendas. The majority of this litigation activity has thus far proceeded outside of the United States, with NGOs and other organizations pursuing companies and financial institutions that they believe are not sufficiently aligned with ESG objectives. In 2021, for example, five NGOs brought a complaint to the SEC alleging misstatements by the Japan International Cooperation Agency regarding "coal-free" bonds, the proceeds of which allegedly could flow to coal-fired power stations in Bangladesh.

More may be on the way. Indeed, the lead lawyer for Milieudefensie, the Dutch wing of the environmental organization Friends of the Earth, which obtained a ruling against Shell in the Netherlands requiring emissions reductions by 2030 (the ruling is on appeal), recently stated: "I think that the next step is to start also litigating against financial institutions who make these emissions and fossil fuel projects possible."

The Materiality Debate Continues

One area that should continue to receive attention is the ongoing debate surrounding what types of ESG information are actually "material" to investment decisions. In securities litigation, where large financial institutions are likely to remain attractive targets in light of the scope of their operations and perceived "deep pockets," liability can turn on the specificity and materiality of the alleged misstatement. Typically, if a statement is deemed vague or aspirational, then courts have found that it cannot have been material to a reasonable investor, and is therefore not actionable. On the other hand, if the statement is concrete enough and would alter the total mix of information that an investor would consider in making an investment decision, then it can potentially support a claim for securities fraud.

Notably, on June 21, 2021, the U.S. Supreme Court issued its decision in Goldman Sachs v. Arkansas Teacher Retirement System, holding that, at the class certification stage, a court may consider whether a company's alleged misstatements were too generic to have impacted its stock price. In advance of the ruling, amicus briefs filed in support of the plaintiff investors argued that generic statements regarding ESG may be material to investment decisions because "investors now incorporate information about a company's ESG performance into their decision-making." As more companies tout their ESG commitments in public disclosures—and as more investors claim to consider such factors when making investment decisions—legal arguments around materiality of these statements should be monitored.

The Debate Over Who Should Police ESG—From Environmental Issues to Human Trafficking

A financial institution's role as a financer, investor, or financial intermediary for a transaction that has ESG-related goals can create the risk of an expectation that a financial institution is responsible for policing those goals, even if that expectation is unreasonable, unwarranted, or unsupported by the transaction documents. Private citizens already have brought claims against banks as financers of third-party projects with negative environmental consequences. A group of residents of Flint, Michigan, for example, sued the underwriters of a municipal water development bond offering, alleging that they knew that the project would cause water contamination in violation of an asserted duty of care owed by the banks to those affected.

Private financial institutions face growing scrutiny in connection with their financing activities in collaboration with international development banks. At least one plaintiffs' lawyer has suggested that banks are a potential target for claims asserting that they have ignored human trafficking-related violations by their customers and derived benefits from facilitating illicit conduct by these customers. Similar claims may also give rise to follow-on shareholder class action cases in the United States and abroad asserting violations of securities laws and/or shareholder derivative claims. As described above, NGOs have already emerged as a formidable constituency seeking to use litigation as a tool to move financial institutions toward a role in policing ESG.

Politicization of ESG: Backlash and the Catch-22 for Financial Institutions

We also continue to monitor efforts by some parties to challenge existing and proposed ESG-related government action, and the partisan nature of these issues. Some state attorneys general may be poised to challenge through litigation various efforts contemplated at the federal level to advance climate and other ESG initiatives, and some have committed to doing so. For example, West Virginia Attorney General Patrick Morrisey sent a letter to the SEC in 2021 describing potential new regulations requiring ESG-related disclosures as unconstitutional. Similarly, in May 2021, the West Virginia treasurer, on behalf of the treasurers of 15 states, wrote to federal Climate Envoy John Kerry to express concern that the Biden administration is reportedly "pressuring U.S. banks and financial intuitions to refuse to lend to or invest in" fossil fuel companies. Separately, in a recent op-ed published in The Wall Street Journal, Arizona Attorney General Mark Brnovich, who is a candidate in the Republican primary for Arizona's U.S. Senate election to be held this November, argued that coordinated efforts to divest from conventional energy resources may amount to an antitrust violation that he and other state attorneys general might pursue.

In 2021, Texas took the lead by enacting two laws targeting financial institutions and other companies that were perceived to economically "boycott" oil and gas businesses. One of the new Texas laws prohibits state pension fund investment in companies deemed by the state comptroller to be boycotting oil and gas companies. Other resource-rich states have passed or are considering similar legislation. Texas has subsequently required financial institutions to submit "anti-boycott"

certifications as prerequisites to engage in underwriting of municipal debt offerings.

In West Virginia, the state legislature recently passed a bill, expected to be signed into law by the governor, that would allow the state treasurer to refuse to enter into or remain in banking contracts with financial institutions that take any action "intended to penalize, inflict economic harm on, or limit commercial relations with a company" because the company engages in fossil fuel-based energy activity. In Kentucky, legislation that would require the state treasurer to maintain a list of financial companies engaged in energy company "boycotts" has passed the Senate and awaits input from the House. Under the proposed legislation, the treasurer's list would be shared with state government entities making investments of more than $1 million annually, which then would be required to cease business with the listed firms.

Highlighting the tensions financial institutions will continue to face in this politically fraught area, recent media reports indicated that the SEC's Fort Worth regional office has opened a preliminary investigation that may be targeting financial institutions that made certifications in connection with the Texas statute. The investigation may involve comparing the certifications against the companies' climate disclosures, emphasizing the challenges to financial institutions trying to navigate in this area. In addition, in June 2021, Maine passed legislation requiring its pension funds to divest from fossil fuels by 2026.

Conclusion

As ESG considerations continue to drive transformative change in the financial markets, they present significant opportunities for financial institutions to support market needs in green finance and elsewhere. The prominence of these issues in industry and in public and political discourse, including in light of the conflict in Ukraine and its impact on world energy markets, however, will continue to bring sustained scrutiny from public and private parties, including regulators, market participants, and NGOs. We will provide updates concerning these issues as they continue to unfold.

Three Key Takeaways

1. Regulators, including the SEC and OCC, are poised to enact new reporting requirements focused on climate risk, among other ESG themes, in the coming months. An increase in enforcement actions is also likely to follow.
2. Financial institutions' ESG-alignment and mitigation of related risks will likely continue to be a major focal point for NGOs and other private stakeholders with increased vigor, given the broader focus on world energy markets in light of the current geopolitical crisis.
3. As more companies tout their ESG commitments in public disclosures—and as more investors claim to consider such factors when making investment decisions—legal arguments around materiality of these statements should be closely monitored.

Jones Day – Jayant W. Tambe, Lizanne Thomas, Mahesh V. Parlikad, Howard F. Sidman, Joseph B. Sconyers and Lauri W. Sawyer

March 21 2022

2nd Suit Targets 'Abusive' CUSIP Licensing Fees, Tactics.

Another suit has been filed in federal court challenging long-standing practices regarding licensing fees regarding the use of CUSIP numbers.

The latest suit was filed March 7 in the Southern District of New York by Hildene Capital Management LLC. As did the suit filed earlier this month, this one involves CUSIPs—those unique identifiers that are used to identify U.S. and Canadian registered stocks, U.S. government and municipal bonds, exchange traded funds and mutual funds. And like the first suit, it alleges that S&P Global, Cusip Global Services (CGS) and the American Bankers Association (ABA)—not to mention an entity called FactSet, which recently took over as GS' new operator—conspired to eliminate competition in the use of CUSIP numbers, or to bring alternatives online.

The suit here also asserts—as did the one filed before it—that "there is nothing original, unique, or special about CUSIP numbers; they are trivial except for the fact they are the standard for identifying financial instruments. Hildene's use of the CUSIP numbers is both necessary and fair because CUSIPs are the designated standard."

The suit, which alleges several violations of federal law,[i] says the essence of the problem is "S&P's abuse of its monopoly power in the financial instruments identification market, and Defendants' conspiracy to maintain S&P's (and now FactSet's) monopoly power and unreasonably restrain trade in the financial instruments identification market, in order to extract artificially inflated payments from investors and other users of financial data through subscription agreements to access CUSIP numbers."

'Hold Up'

The suit explains that these particular plaintiffs "receive no financial data services from Defendants; but rather obtain financial data from other sources that necessarily include CUSIP numbers"—a dependency that the suit says means that the defendants can "hold up" users of the data "to pay prices unilaterally determined by Defendants not because there is anything special or valuable about the string of numbers and letters they generate, but simply because CUSIPs have been designated as the standard."

The suit also alleges that the defendants "have conspired to prevent competition from, and the implementation of, alternative free, or far more cost-friendly financial instruments identifiers of equal or superior efficiency and quality"—motivated by the reality that "CUSIPs are worthless except for the fact that they are the standard."

Fee 'Fie'

It's not as though there isn't already money changing hands here—the suit notes that S&P charges securities issuers a fee (typically about $280 per CUSIP) in order to obtain CUSIP numbers for its securities, and S&P also charges data providers (like Bloomberg), licensing fees for using CUSIPs in its databases (a.k.a. "Data Providers"). However, the sticking point here—and the subject of the suit—is S&P's demand that Data Providers' end users (such as the plaintiffs here)—or "entities that otherwise download CUSIP numbers as part of financial data for their own use" to enter their own subscription agreements with S&P under duress—more specifically, the threat of stripping the CUSIP numbers from their data feeds "if the unilaterally determined licensing fee is not paid."

The suit argues that the ABA retains 30% of CGS's licensing fees from all Data Users and the remainder is kept by S&P (and now FactSet). Meanwhile, the plaintiffs argue that S&P claims that through its CGS division it provides administrative services to Data Users to justify these fees. "However, Data Providers (like Bloomberg), not Defendants, provide these administrative services to Data Users," while—as noted above—the defendants already receive fees for CUSIP numbers twice: first from issuers of securities, and then from the Data Providers. "Defendants' extraction of fees for a third time from Data Users merely because they download financial data that necessarily includes

CUSIPs, does not constitute compensation for administrative services," they note. "Rather, they are demands for payments for a valueless alphanumeric string as part of hold ups monetizing the monopoly power held by virtue of being the standard."

Pressure Tactics

The suit outlines how this impacts data users (like Hildene). Noting first that in Hildene's case this subscription payment amounts was $10,500 annually, the suit goes on to note that "under the threat of stripping CUSIP numbers from the users' data feed. Hildene and the members of the Class are then left with two unenviable options: (i) pay S&P's supracompetitive subscription rates or (ii) have CUSIP numbers stripped from their data feed and suffer, at a minimum, significant disruption to their businesses." Now, when Hildene "balked" at paying these licensing fees, the suit notes that "S&P sent a series of increasingly hostile letters, and eventually constant threats that Hildene must pay the unilaterally set fee or face a debilitating lock out from access to CUSIP numbers. Hildene, with no legitimate business alternative, like other members of the Class, eventually signed the subscription agreement."

But that, as it turns out, is not the end of things. The suit goes on to explain that "S&P's pressure tactics do not end with the signing of a subscription agreement. The form subscription agreement includes a 'Usage Review' provision to inspect a Data User's records concerning the level of usage of the CUSIP identifiers to determine whether additional fees and charges should be imposed." Moreover, there is apparently even a clause that provides S&P with the right to seek reimbursement for the cost of any such inspection if, "in its discretion, the Data User is underpaying by five percent or more."

Beyond that, the suit alleges that S&P reserves the right to increase its fees and change the terms of the subscription agreement. "Without any reasonable choice, the Data User is forced to accept these unfair and deceptive terms," the suit notes. "In sum, S&P is using CUSIPs' designation as the standard and the threat of depriving market participants access to the standard to collect enormous sums of money (and share the money with ABA) from Hildene and members of the Class. It's an abuse of monopoly power, anticompetitive, and simply unfair."

By way of lending support to their arguments (and related attempts to either resolve the current practices and/or to provide alternatives), the suit outlines several attempts to bring the matter (and related concerns) to the attention of the Securities and Exchange Commission (SEC), as well as what it describes as a "similar scheme" in Europe regarding S&P's licensing fee policies for the use of U.S. International Securities Identification Numbers ("US ISINs") in the European Economic Area—an attempt that the European Union found to be an "abuse of monopoly power."

Will there be other suits challenging this structure/fees/practices? Stay tuned.

[i] More specifically, the suit alleges violations of Section 1 of the Sherman Act, Section 2 of the Sherman Act, New York General Business Law § 349(a), Connecticut Unfair Trade Practices Act § 42-110b(a), as well as breach of contract, and injunctive relief. Outside of the class action, Hildene, on its own behalf, also brings this action for a declaratory judgment that Hildene's use of CUSIPs is a "fair use" that does not infringe on any purported intellectual property rights of Defendants over CUSIPs.

NATIONAL ASSOCIATION OF PLAN ADVISORS

BY NEVIN E. ADAMS, JD

MARCH 14, 2022

The S.E.C. Moves Closer to Enacting a Sweeping Climate Disclosure Rule.

The commission gave initial approval to a much-anticipated rule that would require public companies to report the climate-related impact of their businesses.

The Securities and Exchange Commission has said for the first time that public companies must tell their shareholders and the federal government how they affect the climate, a sweeping proposal long demanded by environmental advocates.

The nation's top financial regulator gave initial approval to the much-anticipated climate disclosure rule at a meeting on Monday, moving forward with a measure that would bolster the Biden administration's stalled environmental agenda.

The proposed rule — approved by a 3-to-1 vote — aims to give investors a clearer picture of the risks that climate change might pose to companies, because of disasters like droughts and wildfires, changes in government environmental policies or consumers' declining interest in products that contribute to global warming.

Continue reading.

The New York Times

By Matthew Goldstein and Peter Eavis

March 21, 2022

Cooley: SEC's Climate Proposal - SCOOP!

According to exclusive reporting from Bloomberg, the SEC's new proposal for climate disclosure regulation—scheduled for a vote and release on Monday—will include a requirement to disclose some Scope 3 *emissions*, that is "greenhouse gases that are generated by other firms in [a company's] supply chain or by customers using [its] products." It's widely believed that Scope 3 emissions "make up the bulk" of most companies' emissions. It's unclear whether the proposed requirement would apply to all public companies or just larger ones, or whether the requirement might be phased in. As discussed below, whether or not to require disclosure of Scope 3 emissions has been a subject of heated internal debate at the SEC, and, the article suggests, the proposal appears to reflect some compromise.

The article indicates that the rules will require companies to discuss "indirect emissions that are 'material' to their operations. Because of the legal uncertainty surrounding the term, the proposal is likely to provide examples for companies to follow, [sources said]. The commissioners also compromised on whether the new corporate filings will need to be audited, another flashpoint. The regulation is likely to require expert review, but it will be phased in over time, the people said." Note that the frequently mentioned framework of the Task Force on Climate-Related Financial Disclosures provides for disclosure of Scope 3 emissions "if appropriate," which could suggest a materiality test.

As noted above, the wrangling over whether to require disclosure regarding Scope 3 emissions has been fierce—including among the commissioners. Back in January, Reuters reported that environmentalist and some activist investors were strongly advocating that the SEC require companies to make broad disclosure about GHG emissions, while business groups were "pushing for a narrower rule that will make it easier and less expensive to gather and report emissions data, and which will protect them from being sued over potential mistakes." The article reported that a "major issue staff are struggling with is whether and how some or all companies should disclose the broadest measure of greenhouse-gas emissions, also known as 'Scope 3' emissions, according to the sources and company and investor advocates." Another "big challenge" that the article highlighted was "identifying which Scope 3 metrics help investors gauge a company's financial prospects, and ensuring the rule is flexible enough to generate specific, rather than generic information." While activists may view Scope 3 emissions disclosure as "critical," some companies contended that "there is no agreed methodology for calculating Scope 3 emissions and providing that level of detail would be burdensome." In addition, they maintained, this information was not necessarily within each company's control and exposed companies to potential litigation.

The Reuters article discussed some compromises the staff was considering at the time, including whether to create a new safe harbor or to rely on the current safe harbor for forward-looking statements. One alternative under consideration was reportedly to require some information about Scope 3 emissions to be filed as part of companies' financial reports and other Scope 3 data to be submitted separately. The article reported that the staff had reached out to advocacy groups such as Ceres and Public Citizen for feedback on Scope 3 issues, including phase-ins and safe harbors. A Ceres representative indicated that the SEC had solicited his views on "whether it should include Scope 3 for large, high-revenue companies, then phase in medium and small-sized companies a year or two later." Time will tell whether any of these compromises will be included in the ultimate proposal. (See this PubCo post.)

And in February, Bloomberg reported that one of the reasons for the delay in the release of the SEC's climate disclosure proposal was internal conflict about the proposal—conflicts not between the Dems and the one Republican remaining on the SEC; rather, they were reportedly between SEC Chair Gary Gensler and the two other Democratic commissioners, Allison Herren Lee and Caroline Crenshaw, about how far to push the proposed new disclosure requirements, especially in light of the near certainty of litigation, and whether to require that the disclosures be audited. The article painted the SEC's dilemma about the rulemaking this way: "If its rule lacks teeth, progressives will be outraged. On the flip side, an aggressive stance makes it more likely the regulation will be shot down by the courts, leaving the Biden administration with nothing. Either way, someone is going to be disappointed."

According to the Bloomberg article, the issues centered around "how much information the agency can force companies to divulge without losing an almost certain legal challenge brought by Washington's business lobby or a Republican-led state. Fundamental to the debate, Bloomberg indicated, was the question of "materiality." (See this PubCo post for a discussion of the some of the commissioners' views of "materiality.") The authors reported that Gensler had "caution[ed] agency staff to make sure the climate proposal adheres to a legally defensible definition of materiality. He contend[ed] that only this approach can survive a legal challenge." According to the reporters' sources, "[t]ensions over the divergent approaches have reached a tipping point.…At one meeting,… Gensler told SEC lawyers that their work must conform with the interpretation of materiality that has been laid out by the U.S. Supreme Court—a standard that underpins the SEC's guidance. Gensler made clear that, as far as he was concerned, there would be no more debate on the issue," the sources told Bloomberg. (See this PubCo post.)

Some contend that litigation is inevitable, regardless of what the proposal requires, and Bloomberg has reported that "[m]ost Republicans insist that regulating global warming is outside the agency's jurisdiction, and business groups have already been discussing a litigation strategy." The WSJ has also reported that some Republicans argue that "it isn't the SEC's job to mandate nonfinancial disclosures." In addition, the article continues, some industry organizations "told the SEC it didn't have legal authority to compel disclosures and impose its value judgments." One Republican state attorney general "wrote that 'West Virginia will not permit the unconstitutional politicization of the Securities and Exchange Commission. If you choose to pursue this course we will defeat it in court.'"

> **SideBar**
> According to a 2021 report from Deloitte of a 2021 survey of audit committee members globally, not that many companies had planned to disclose Scope 3 emissions. In the Americas, only 26% of respondents said they were reporting or planning to report Scope 3 emissions as part of their TCFD disclosures. Companies that were planning to report Scope 3 identified as the biggest challenges the ambiguity of measurement standards (92%), lack of robust information from the value chain (85%), lack of clear parameters to define Scope 3 emissions (77%), lack of understanding of the perceived value of this information (62%) and lack of co-operation from the parties in the value chain (46%). Deloitte observed that, while the entire task of addressing climate is enormous, "Scope 3 GHG emissions are significantly more difficult to quantify than those in Scope 1 or 2." However, Deloitte asserted, given that "Scope 3 emissions are likely to be the most material part of a company's carbon footprint, companies need to get more comfortable with preparing and exchanging information to facilitate greenhouse gas reporting in the value chain." (See this PubCo post.)

Of course, the SEC still has a few days before the meeting—time enough to make further changes in the proposal. How the proposal will ultimately shake out remains to be seen.

Cydney Posner on March 18, 2022

Cooley LLP

SEC Charges Texas School District and Former CFO with Fraud Related to Bond: Faegre

On March 16, 2022, the Securities and Exchange Commission charged Crosby (Texas) Independent School District (Crosby) and its former Chief Financial Officer, Carla Merka, with misleading investors in a $20 million municipal bond sale, which was issued to pay down outstanding construction liabilities and fund new construction projects.

The SEC's civil complaint alleges that Crosby failed to disclose $11.7 million in payroll and construction liabilities in connection with the January 2018 sale. The complaint also alleges the school district falsely reported that its general fund had $5.4 million in reserves in its 2017 fiscal year financial statements. According to the Complaint, Merka, who had ultimate authority over Crosby's fiscal year 2017 financial statements and was its highest-ranking executive with financial or accounting experience, was aware that Crosby's financial statements significantly underreported its existing liabilities and that she knowingly included the statements in the bond offering documents.

In August 2018, seven months after the bond sale, Crosby's leadership disclosed its financial difficulties. The disclosure led to employee layoffs for the school district and the downgrading of Crosby's bonds.

Crosby's auditor, Shelby Lackey, was also charged with improper professional conduct in connection with an audit of the school district's 2017 financial statements. Specifically, the SEC alleged Lackey violated the Generally Accepted Auditing Standards (GAAS) by failing to obtain adequate evidence to verify Crosby's payroll and construction liabilities, failing to supervise the audit, and failing to exercise professional judgment and maintain professional skepticism.

Crosby consented to the entry of an order to settle the SEC charges on a no-admit, no-deny basis. The order finds that Crosby violated the anti-fraud provisions of the federal securities law. The order cites Crosby's remedial acts and cooperation with the SEC in ordering it to cease and desist from future anti-fraud violations. Lackey also agreed to settle the SEC's charges and consented to the entry of an order that, without admitting or denying any of the findings, suspends her from appearing or practicing before the SEC as an accountant with the right to apply for reinstatement after three (3) years. Merka agreed to pay a $30,000 penalty and to not participate in future municipal securities offerings. In an apparent attempt to highlight her primary role in the false reporting, the SEC effectuated the settlement with Merka through pleadings filed in the civil lawsuit, as opposed to the other parties who were allowed to settle via administrative orders.

This action highlights the SEC's efforts and approach in enforcing securities laws in the context of municipal bond offerings. In 2021, the Division of Examinations stated it would prioritize investments heavily used by retail investors or those that may present elevated risks, including municipal securities. See https://www.sec.gov/news/press-release/2021-39. Those involved in such offerings should consult experienced legal counsel in connection with preparing their offering materials, and particularly in any interaction with the SEC Division of Enforcement, in the event it commences an investigation or enforcement action.

by Michael R. MacPhail, Isaac Smith

March 21, 2022

Read the Responses to the MSRB's RFI on ESG Practices in the Muni Market.

The MSRB invited stakeholders to provide their perspectives on ESG disclosures and ESG-labeled bonds.

Read the responses.

MSRB RFI on ESG Practices in the Municipal Securities Market: SIFMA Comment Letter

SUMMARY

SIFMA provides comments to the Municipal Securities Rulemaking Board (MSRB) on their Notice (MSRB Notice 2021-17) requesting public input on environmental, social and governance (ESG) practices in the municipal securities market. The MSRB is seeking this input as part of its broader stakeholder engagement on ESG trends in the municipal securities market and to help inform its mandate of protecting investors, municipal issuers, and the public interest by promoting a fair, efficient and transparent municipal market.

Read the SIFMA Comment Letter.

BDA Joins Eight Municipal Market Advocacy Groups in Filing Joint Comment Letter on MSRB's Notice on ESG-Labeled Municipal Securities.

Read the Comment Letter.

Bond Dealers of America

MARCH 10, 2022

Market Response to MSRB ESG Survey Shows Frustration.

The Municipal Securities Rulemaking Board's request for information on environmental, social and governance considerations has elicited irritation at the board's attempt to regulate ESG matters and illustrated the challenges the board faces in trying to decide what if any steps it might take related to ESG.

The comment period for the RFI ended on Tuesday and the challenges ahead will be even more pressing now that the board kicked off its fact-finding mission to much industry fervor. Initial comments indicated that standardized ESG disclosures would add quite the workload for issuers, as was previously indicated in the Government Finance Officers Association's best practices on ESG, a document the group touched on significantly in its own submission.

But the board collected a total of 36 submissions from issuers, individuals, and industry groups that outline clearly the limits the board faces.

"We all agree that a bright line exists in practice between (i) the ESG risk-based disclosures that relate to and have a nexus to all credits and obligations, (ii) the process designated/labeled bonds and (iii) the disclosures that relate to and are requested by investors for such designated/labeled bonds," said the Disclosure Industry Working Group's joint letter, signed by the Securities Industry and Financial Markets Association, Bond Dealers of America, National Association of Municipal Advisors, National Association of Bond Lawyers, among many others, and led by the Government Finance Officers Association.

"It is important not to confuse or actively conflate these topics because each is different," the joint letter said.

Many of the letters the MSRB received note the fact that the board is responsible for regulating broker-dealers and municipal advisors and that any regulations attempting to add a disclosure

burden or to establish materiality should be reserved for the Securities and Exchange Commission.

“The MSRB does not have the authority to determine materiality and the content of issuer disclosures and market participant preferred activity, outside of the MSRB’s own rules over broker-dealers and municipal advisors,” the DIG letter said.

“While the board is charged with protecting issuers and investors, that authority is limited to the regulation of municipal securities dealers and municipal advisors, neither of whom have control over issuer disclosure documents or issuer ESG designation practices,” the Bond Dealers of America letter said. “This lack of authority means there is no meaningful action the MSRB could take to address any hypothetical issues associated with issuer ESG designations, so the purpose of the notice is unclear.”

But there are some things that respondents feel the board can do to help ESG investments in the muni market to become more transparent.

“There are many areas where the MSRB can contribute to the ESG conversation and where their authority rests,” the DIG joint letter said. “The primary contribution would be to improve EMMA and allow for disclosures to be readily entered and accessed,” the DIG letter said. “We cannot emphasize enough our consensus on this point and the need for general EMMA improvements to occur.”

Respondents were also quick to point out that if regulators want to get serious about ESG, referring to concepts generally is probably not going to win over the muni market.

“The RFI continues to reference these types of issuances as “ESG-Labeled Bonds” which is a misnomer as there is presently no such label,” the GFOA letter said. But that term is used throughout the market generally to discuss the topic of green or social bonds. Respondents urge the board these matters are disclosed and discussed separately.

“It is imperative to ensure that the topics of designated bonds, disclosures related to designated bonds, and general disclosure of ESG factors are kept separate,” the GFOA letter said. “Going forward, these discussions should be held separately from one another since they are about two very different concepts.”

Many of the issuer respondents disclose some information to credit ratings agencies, as the information provided often doesn’t differ much from what is provided in offering documents and does have a material effect on ratings. But when it comes to bond designations, some feel that a third-party opinion doesn’t matter, given how quickly the market for ESG investments is changing.

The New York City Housing Development Corporation, an issuer of both green and social bonds, doesn’t feel the need to get a third-party opinion on its bond designations because “it is not necessary to market HDC’s bonds and the market is constantly evolving,” Ellen Duffy, executive vice president of debt issuance and finance at the New York Housing Development Corporation said in a letter.

“Also, issuers do not see any pricing benefit of marketing ESG bonds to warrant this extra expense,” she added.

While the fact that bond designations don’t add any pricing benefit has been observed, others in the market are seeing it differently.

“Our members are beginning to see that in some cases, an ESG designation on a bond may affect pricing, suggesting that the designation is material information,” the BDA letter said.

But the NYCHDC does plan to provide annual updates connected with the disbursement of the proceeds for its Sustainable Development Bonds and the financing of mortgage loans, of which the reporting is completely separate from its obligations under its Continuing Disclosure Agreement.

The New Jersey Infrastructure Bank issued green bonds and like the NYCHDC, follows guidance from the International Capital Market Association. The Official Statement for any green bond issuance includes a use of proceeds section, but the NJIB has further suggestions for how issuers could handle disclosing this type of information.

“Municipal issuers could include a separate section in their Official Statement and other offering documents expressly devoted to ESG-Related Disclosures,” the NJIB letter said.

The letter even goes even further to suggest the MSRB take a larger role in disclosure, departing from many of the submissions where respondents felt that such a move would be overstepping its mandate. “Guidance from MSRB for content would be helpful to establish guidelines about what should be reported.”

The State of Florida Division of Bond Finance has not issued any designated bonds but agrees that some ESG-related information should be included in offering documents, as they include an “environmental risk factors” disclosure in addition to an “information technology security” disclosure. But these weren’t considered as part of the ESG movement when Florida began to include them in offering documents.

“Municipal issuers have customarily provided this kind of information long before it was categorized as ‘Governance’ or ‘Social’ within the ESG moniker,” said Ben Watkins, director of bond finance for the State of Florida in his letter.

“We do not feel that rearranging or renaming sections of offering documents as ‘ESG’ is necessary to meet the information needs of investors,” he added. “If the relevant information disclosure information is included in a rational order and easy to follow, it should not require a label for investors to locate it within the offering document.”

The RFI has offered the muni market an outlet to share ESG experiences, but what the board plans to do with this information is another question.

“MSRB has not established a roadmap for what it intends to do with the information gathered in this exercise or even possible options – perhaps because it has no legitimate role,” the National Association and Educational Facilities Finance Authorities letter said. “The MSRB’s considerable resources should be focused on regulatory issues relating to the regulated entities it oversees – not issuers/borrowers – and making enhancements and improvements to EMMA which all sectors of the public finance community have been imploring be undertaken for many years.”

By Connor Hussey

BY SOURCEMEDIA | MUNICIPAL | 03/09/22 12:30 PM EST

SIFMA Statement on Inclusion of LIBOR Legislation in the Omnibus.

Washington, D.C., March 9, 2022 – SIFMA released the following statement from president and CEO Kenneth E. Bentsen, Jr., on the inclusion of the Adjustable Interest Rate (LIBOR) Act in the omnibus

in the U.S. House of Representatives today:

“We commend the inclusion the Adjustable Interest Rate (LIBOR) Act, sponsored by Representative Brad Sherman (D-CA) and Senators Jon Tester (D-MT) and Thom Tillis (R-NC), in the Consolidated Appropriations Act of 2022.

“There are currently trillions of dollars of existing contracts and instruments that, as a practical matter, cannot be amended to utilize an alternative rate and Federal legislation is necessary to facilitate a smooth transition away from LIBOR to an alternative reference rate for these ‘tough legacy’ contracts. This legislation will benefit all market participants including LIBOR’s end users, who range from investors to companies to consumers.

“The legislation would provide four key benefits: (1) certainty of outcomes; (2) fairness and equality of outcomes; (3) avoidance of years of paralyzing litigation; and (4) preservation of liquidity and market resilience, and accordingly is supported not only by SIFMA, but also a range of other market participants, consumer groups, and regulators.

“We encourage the House and Senate to quickly pass this much-needed legislation so it will reach the President’s desk soon.”

SIFMA Statement on Senate Passage of LIBOR Legislation.

Washington, D.C., March 10, 2022 – SIFMA released the following statement from president and CEO Kenneth E. Bentsen, Jr., on the passage of the Adjustable Interest Rate (LIBOR) Act by the U.S. Senate:

“We commend the Senate’s bipartisan passage of the Adjustable Interest Rate (LIBOR) Act, sponsored by Senators Jon Tester (D-MT) and Thom Tillis (R-NC), with Chairman Brown (D-OH), Ranking Member Toomey (R-PA) and Representative Brad Sherman (D-CA).

“LIBOR will cease publication next year and there are currently trillions of dollars of existing contracts and instruments that, as a practical matter, cannot be amended to utilize an alternative rate. Federal legislation is necessary to facilitate a smooth transition to an alternative reference rate for these ‘tough legacy’ contracts. This legislation will benefit all market participants including LIBOR’s end users, who range from investors to companies to consumers.

“The legislation provides four key benefits: (1) certainty of outcomes; (2) fairness and equality of outcomes; (3) avoidance of years of paralyzing litigation; and (4) preservation of liquidity and market resilience, and accordingly is supported not only by SIFMA, but also a range of other market participants, consumer groups, and regulators.

“We appreciate both the House and the Senate’s swift passage of this important bill and encourage the signing of this much-needed legislation into law.”

LIBOR Act Protects US Legacy Contracts; New SOFR Use Growing - Fitch

Fitch Ratings-London/Milan/New York-11 March 2022: The Adjustable Interest Rate (LIBOR)

Act provides strong protection for legacy contracts without workable fallback provisions, significantly reducing transition and disruption risk upon eventual USD LIBOR phase-out, Fitch Ratings says. The shift away from LIBOR for new issuance continues apace, with SOFR dominating new floating-rate issuance in 2022. Congress passed the LIBOR Act yesterday as a part of the Consolidated Appropriations Act, 2022.

The act requires SOFR plus a set spread, depending on the LIBOR term, to be used instead of USD LIBOR starting from mid-2023. The act applies to contracts with no or impracticable LIBOR fallback provisions, contracts that lack a specific alternative rate and those for which the determining person has not replaced the benchmark by the date required under the contract or mid-2023. By providing a defined alternative to LIBOR for contracts issued under US law, the act would result in consistent rates for a substantial portion of floating-rate bond and loan markets.

The act also provides contract continuity and safe-harbor provisions to shield parties from liability under potential lawsuits due to the transition away from LIBOR. Even if ultimately unsuccessful, litigation could be disruptive for transactions with affected contracts, particularly from consumer loan class-action lawsuits.

The Federal Reserve Board must issue regulations to administer the law within 180 days of passage, and operational challenges could arise in implementation. Conforming changes necessary to apply a replacement rate, such as updating where the new rate is published, are protected under the act; therefore, we consider these changes low risk for transaction parties. However, there remains a risk that parties may delay or have difficulty making the conforming changes. For consumer loan contracts, only conforming changes approved by the Fed are allowed and would be covered under the act. Regulations should clarify how this will be implemented.

For Federal Family Education Loan Program (FFELP) student loan asset-backed securities (SL ABS) LIBOR exposure, the act amends the Higher Education Act of 1965 to allow the LIBOR rate for special allowance payments to be substituted by SOFR plus a spread. The new rate will apply following certain notifications by the holder to the Secretary of Education, but if the notification does not occur by certain dates, the SOFR rate will automatically apply. Legacy LIBOR FFELP ABS notes are also expected to convert to a SOFR reference rate, so the risk of significant interest rate mismatches between assets and liabilities is mitigated.

US banks may use any reference rate other than LIBOR for loans, provided that management determines it is appropriate based on its funding model and customer needs. We expect some banks, particularly community and regional banks, to opt to use credit-sensitive benchmarks such as the American Financial Exchange’s Ameribor or Bloomberg’s Short-Term Bank Yield Index in lieu of SOFR, which may result in a multi-rate environment in the US. However, as the SOFR debt pipeline builds, so does the depth and liquidity of SOFR swap trading, which may mean the market coalesces around SOFR over time.

Since the start of 2022, new issuance in several markets has overcome the challenge of determining an agreed spread adjustment when moving from a LIBOR to SOFR reference rate. We have seen increasing issuance of leveraged loans and CLO notes referencing SOFR and more are expected.

Legacy contracts with fallback provisions that reference non-LIBOR rates such as prime or federal funds are not covered by the act, but are also likely to see minimal disruption risk if they have hardwired fallback language in line with recommendations from the Alternative Reference Rate Committee (ARRC). Standard leveraged loan documents have provided for the automatic conversion to a non-Libor rate, but conversion to a higher rate could pressure corporate interest coverage.

The Bond Pricing Institute, a Division of the BDA, Announces Steering Committee and 2022 Agenda.

View the BPI Announcement.

Bond Dealers of America

MARCH 8, 2022

GASB Requests Proposals for 2022 Crain Research Grants.

Read the GASB Request for Research.

03/10/22

MSRB Publishes 2021 Fact Book of Municipal Securities Data.

Washington, DC – The Municipal Securities Rulemaking Board (MSRB) today published its annual Fact Book, the definitive compilation of the most recent five years of statistics on municipal market trading, interest rate resets and disclosures. The data in the 2021 Fact Book can be further analyzed to identify market trends.

The MSRB collects real-time municipal securities trade data, as well as primary market and secondary market disclosures. In addition to making the data and disclosures available for free on its Electronic Municipal Market Access (EMMA®) website and compiling quarterly and annual statistics, the MSRB conducts independent research and analysis to support understanding of market trends. Recent MSRB research examines the use of external and internal liquidity in the municipal market; assesses the impact of electronic trading technology in the market; and studies the evolution of the taxable municipal bond market.

“With the 14th edition of the Fact Book, the MSRB is continuing its commitment to equip municipal market participants, policymakers, regulators, academics and others with information to understand long-term and emerging trends in our market,” said MSRB Director of Research Marcelo Vieira. “We are exploring and prototyping new, more dynamic ways to make market data available to the public in our new EMMA Labs innovation sandbox. We welcome feedback from stakeholders about how to enhance future editions of the Fact Book, perhaps ultimately replacing this static publication with a truly dynamic data dashboard that gives users greater flexibility to access and analyze the data throughout the year.”

EMMA Labs is a key part of the MSRB’s long-term strategic goal to leverage data to deepen market insights. One of the first prototypes available for users to explore in EMMA Labs is a dynamic dashboard for market data analysis that empowers users to discover and visualize market trends.

Highlights from the 2021 Fact Book include:

- A significant decline in par amount traded and number of trades in 2021 to the lowest levels since

2006. Par amount traded was down 28% in 2021 compared to 2020, while the number of trades decreased 10%.
- Persistent strength in trading of taxable securities, continuing the trend started in 2020, with taxable securities accounting for about 17% of the par traded in 2021, compared to 14% in 2020.
- A slight decrease in primary and continuing disclosures submitted to the MSRB in 2021. Primary disclosures were 13,697 in 2021, down from 13,914 in 2020, while continuing disclosures fell slightly to 156,294 in 2021 from 156,847 in 2020, largely as a result of a 3% decline in event-based submissions.

The 2021 Fact Book includes monthly, quarterly and yearly aggregate market information from 2017 to 2021, and covers different types of municipal issues, trades and interest rate resets.

Date: March 3, 2022

Contact: Leah Szarek, Chief External Relations Officer
202-838-1300
lszarek@msrb.org

Hawkins Advisory: New Private Activity Bond Provisions for Qualified Carbon Dioxide Capture Facilities

A new category of tax-exempt private activity bonds was created as part of the Infrastructure Investment and Jobs Act, enacted in November 2021, to encourage private investment in carbon dioxide capture facilities. The attached Hawkins Advisory attempts to describe and explain the applicable provisions.

Read the Hawkins Advisory.

Joint Trades Letter in Support of LIBOR Legislation to Address "Tough Legacy" Contracts - SIFMA

SUMMARY

SIFMA in a joint letter with other associations provided comments to the Senate to quickly pass the much-needed LIBOR legislation. We, the undersigned organizations, support the Economic Continuity and Stability Act, sponsored by Senators Tester and Tillis with Chairman Brown and Ranking Member Toomey to address “tough legacy” contracts that currently reference LIBOR.

SIFMA signed with the following:

Structured Finance Association
Bank Policy Institute
Commercial Real Estate Finance Council (CREFC)
Institute for Portfolio Alternatives
Government Finance Officers Association
Student Loan Servicing Alliance
The Real Estate Roundtable

Education Finance Council
The Financial Services Forum
The Loan Syndications and Trading Association (LSTA)
Institute of International Bankers
Mortgage Bankers Association
The International Swaps and Derivatives Association (ISDA)
Independent Community Bankers of America
National Association of Corporate Treasurers
U.S. Chamber of Commerce, Center for Capital Markets Competitiveness
Consumer Bankers Association
Housing Policy Council
Investment Company Institute
American Bankers Association
The American Council of Life Insurers (ACLI)
Mid-Size Bank Coalition of America

Headlines for Alternative Lenders on LIBOR Replacement: McGuireWoods

The LIBOR Transition Continues

While Dec. 31, 2021 was a key LIBOR transition deadline for many lenders, the transition has continued in 2022 with alternative lenders in particular continuing to use the LIBOR tenors that will remain available until June 30, 2023. Lenders continue to explore different benchmark alternatives, from two- or three-part calculations for day one SOFR calculation to several emerging versions of "credit sensitive rates" that share operational similarities with LIBOR, which can have a material effect on the return on loans and negatively impact the efficiency of the capital markets. In multicurrency deals, the number of applicable benchmarks has multiplied, further complicating yield calculations. For more information, see "Banks Press Ahead with Term SOFR Preparation; Credit Sensitive Rates Under Scrutiny."

Hidden Costs of Reference Rates

Use of the LIBOR reference rates required a license with ICE Benchmark Administration (IBA), the administrator of the LIBOR reference rate. Replacement reference rates are likely to require a license with **each administrator of the applicable reference rate**. For more information, see "Banks Press Ahead with Term SOFR Preparation; Credit Sensitive Rates Under Scrutiny."

Beware Loan Documents Without Replacement Rates for LIBOR

The states of New York and Alabama have enacted laws with default benchmark rates for contracts governed by their state laws that do not include clearly defined or practicable LIBOR replacement benchmark rate provisions. A lender party to the rare New York or Alabama governed credit or loan agreement with LIBOR provisions but no default replacement rates for the LIBOR provisions could suddenly experience a drastic, unexpected change in the economics under that credit or loan agreement. For more information, see "LIBOR Legislation Bill Passed by New York State Legislature."

Key LIBOR Expiration Dates

All LIBOR settings have ceased, or will cease, to be provided by any administrator or no longer will

be representative after:

- Dec. 31, 2021, in the case of all sterling, euro, Swiss franc and Japanese yen settings, and the 1-week and 2-month U.S. dollar settings; and
- June 30, 2023, in the case of the remaining U.S. dollar settings.

McGuireWoods LLC

March 4, 2022

New and Familiar Compliance Challenges for FINRA Members in 2021 and What That Means for 2022: Katten Muchin Rosenman

Payment for order flow (PFOF) and best execution; market access; finfluencers and gamification; and anti-money laundering were some of the most critical emerging and familiar compliance challenges faced by member firms addressed by the Financial Industry Regulatory Authority (FINRA) in 2021 through relevant guidance and its enforcement program.

Looking into 2022, FINRA is expected to continue to pay careful attention to compliance issues surrounding these challenges, as well as those newly identified in the authority's 2022 Report on Examination and Risk Monitoring Program.1 These include firm short positions and fails-to-receive in municipal securities; trusted contact persons; funding portals and crowdfunding offerings; disclosure of routing information; and portfolio margin and intraday trading.

This review elaborates in detail on top emerging and compliance challenges of members addressed by FINRA in 2021 and reviews additional 2022 issues that also may be targeted by FINRA.

Payment for Order Flow (PFOF) and Best Execution
In June 2021, FINRA issued Regulatory Notice 21-23 (Best Execution and PFOF), which reminded firms of their obligations with respect to PFOF2 and best execution.

Generally, FINRA Rule 5310 requires FINRA members to "use reasonable diligence to ascertain the best market for a security, and to buy or sell in such market so that the resultant price to the customer is as favorable as possible under prevailing market conditions." Regulatory Notice 21-23 made clear that PFOF arrangements do not alter a firm's best execution obligations, and to meet such obligations a firm must compare execution quality obtained from existing arrangements against quality that could be obtained from competing markets.

Securities and Exchange Commission (SEC) Chairman Gary Gensler recently sent a directive to SEC staff to consider whether additional best execution requirements or guidance are needed to promote investor protection, hinting at future developments in this area.3

In the past year, FINRA fined three firms for purported best execution violations, resulting in approximately $1.5 million in fines. In particular, FINRA assessed a fine of $850,000 against a member firm for allegedly failing to exercise reasonable diligence to ensure that it routed customer orders through venues that provided the best execution quality.4 FINRA found the firm prioritized the routing of marketable equity orders to market makers and exchanges that paid for that order flow or paid the highest rebates.

FINRA also found the firm failed to reasonably supervise for best execution; specifically, its written

supervisory procedures (WSPs) provided no guidance as to how the supervisor should conduct an execution quality analysis of competing markets.

In addition, FINRA fined another member firm $575,000 for supposedly violating best execution obligations in connection to its role as a market maker in over-the-counter (OTC) securities.5 FINRA said the firm "[failed] to use reasonable diligence to ascertain the best market for the subject securities and [failed] to buy or sell in such a market so that the resultant prices to the customers were as favorable as possible under prevailing market conditions."6 The manual process used by the firm for comparing customer orders resulted in the firm, at times, missing better-priced messages and not executing orders at the best available price.

FINRA also determined that there were shortcomings in the firm's supervisory system — the firm did not account for price opportunities available through its electronic messaging service and thus had no way to determine if its customer orders received inferior executions to those available via the messages.

Further, FINRA fined a third member firm $80,000 for purportedly failing to comply with best execution obligations under FINRA Rule 5310. Specifically, FINRA found that the firm failed to "use reasonable diligence to ascertain the best market for a subject security and buy or sell in such market so that the resultant price to the customer was as favorable as possible under prevailing market conditions in connection with 26 corporate bond transactions."

In addition, FINRA also found that the firm failed to establish and maintain a supervisory system designed to comply with FINRA Rule 5310, fining the firm an additional $20,000.7

With respect to PFOF, FINRA fined a member firm $170,000, claiming the firm failed to disclose material aspects of its PFOF arrangements, among other things. Additionally, FINRA concluded that the firm did not establish and maintain a supervisory system, including WSPs, reasonably designed to achieve compliance with disclosure obligations pertaining to PFOF under Regulation NMS (Reg NMS) Rule 606.8 Although the firm's Rule 606 report9 in Q1 of 2018 stated that it may receive and/or make payments in varying amounts from the exchanges or other broker-dealers, FINRA said the report failed to disclose the material aspects of its relationship with its significant execution venues, including descriptions of any PFOF arrangements.

Market Access

Rule 15c3-5 of the Securities Exchange Act of 1934 (the Market Access Rule) requires broker-dealers providing market access (i.e., access to trading in securities on an exchange or alternative trading system) to establish, document and maintain a system of risk management controls and supervisory procedures reasonably designed to manage financial, regulatory and other risks of the business.

FINRA reported five market access cases in 2021, totaling approximately $1.67 million in fines.

FINRA's market access cases can generally be distinguished by settlement amounts: (1) settlements above $1 million, which typically involve violations of multiple rules, including anti-money laundering (AML) violations, over a long period of time; (2) settlements around $300,000–$500,000, which involve a limited number of violations or affected transactions; and (3) settlements around $50,000, which generally involve minor procedural violations. An example of a market access case from each of the three categories above is highlighted below.

First, FINRA and various self-regulatory organizations (SROs) fined a member firm $1.25 million for, among other violations, allegedly failing to establish and maintain a supervisory system and

regulatory risk management controls reasonably designed to monitor for potentially manipulative trading, such as potential layering, spoofing, wash trades, prearranged trades, marking the close and odd-lot manipulation.10

Importantly, FINRA and the SROs did not determine the firm failed to detect actual instances of manipulative trading — rather, they found that the firm's failures concerning the Market Access Rule resulted in potentially manipulative trading.

FINRA also found the firm failed to implement a reasonably designed AML program for the detection and reporting of potentially suspicious transactions. Specifically, FINRA claimed the firm's written AML procedures did not address potentially manipulative trading at all. These violations allegedly continued for a period of 10 years.

Second, FINRA fined a brokerage firm $310,000 for purportedly failing to comply with various provisions of the Market Access Rule for a period of under two years relating to establishing, monitoring, and amending customer credit limits and conducting annual reviews and certifications of the effectiveness of its market access risk management controls and supervisory procedures.11 FINRA said the firm's WSPs "did not include reasonably designed procedures for customer credit limits because they did not require firm personnel to conduct due diligence as to the customer's business, financial condition or trading patterns."12

Third, FINRA fined a broker-dealer $40,000, claiming that it failed "to establish financial risk management controls and supervisory procedures to systematically limit its financial exposure that could arise as a result of market access."13 For example, FINRA said the firm did not have any pre-trade controls to prevent the entry of orders that exceed preset credit or capital thresholds for customers. Because the purported violations were mostly procedural, FINRA assessed a lower fine.

Common market access issues across firms include failing to establish WSPs or having insufficient WSPs, failing to supervise for manipulative orders, failing to conduct an annual review of its business activity in connection with market access, and AML violations.

Finfluencers and Gamification

Exam Sweep of Broker-Dealer Practices Related to "Finfluencers" (Sept. 2021)

In September 2021, FINRA published guidance entitled "Social Media Influencers, Customer Acquisition, and Related Information Protection,"14 notifying member firms that FINRA is conducting a review of broker-dealer practices related to the acquisition of customers through social media channels.15 According to the guidance, the exam sweep focuses on firms' supervision and communications related to paid social media influencers. The sweep inquiry letter poses multiple questions and subparts, including requests for details regarding firms' relationships with social media influencers, including how they are found and compensated, information on any referral programs in which the firms may be engaged, and WSPs around the use of social media influencers.

Annual Report on Examination and Risk Monitoring Programs (Feb. 2021)

In February 2021, FINRA released its annual report on "Examination and Risk Monitoring Program,"16 which highlighted "gamification" as an emerging risk.17 Gamification features include "a range of technologies and techniques designed to influence investor behavior, including 'games' at sign-up; social networking tools; streaks with prizes, such as free stock; points, badges and leaderboards; and push notifications."18 The annual reports warned broker-dealers of their existing regulatory obligations, including compliance with Regulation Best Interest (Reg BI), supervisory and

diligence obligations, and various FINRA communications rules. Specifically, the guidance noted that broker-dealers must evaluate gamification features to determine whether they meet regulatory obligations to:

- comply with any Reg BI and Form CRS requirements if any communications constitute a "recommendation" that requires a broker-dealer to act in a retail customer's "best interest;"
- make disclosures relating to risks to customers, fees, costs, conflicts of interest, and required standards of conduct associated with the firm's relationships and services;
- prohibit the use of false, exaggerated or misleading statements or claims in any communications and ensure all firm communications are fair and balanced and do not omit material information concerning products or services;
- comply with account opening requirements that require firms to gather information about customers and approve certain types of accounts, including options accounts;
- develop a comprehensive supervisory system for such communication methods, including surveilling for red flags of potential violative behavior, and maintaining books and records of all communications related to the firm's business as such; and
- address compliance with FINRA communications rules.

While no enforcement action has been brought by FINRA to date concerning the use of finfluencers or gamification sales practices, member firms in 2022 can expect to see enforcement activity related to potential violations of Reg BI, suitability obligations, communication standards (which require all member communication to be fair and balanced), and supervision.

Anti-Money Laundering (AML)

FINRA Rule 3310 requires member firms to develop and implement a written AML program reasonably designed to achieve and monitor compliance with the requirements of the Bank Secrecy Act of 1970 (BSA) and its implementing regulations. The BSA and related regulations impose a number of requirements, including "implementing and maintaining both AML programs and Customer Identification Programs (CIPs); filing reports of suspicious activity; verifying the identity of legal entity customers; maintaining procedures for conducting ongoing customer due diligence; establishing due diligence programs to assess the money laundering risk presented by correspondent accounts maintained for foreign financial institutions; and responding to information requests from the Financial Crimes Enforcement Network within specified timeframes."19 In 2021, FINRA brought 12 cases against member firms and individuals for violations of Rule 3310, three of which are highlighted below.

Most notably, FINRA fined a prominent broker-dealer $57 million for several purported violations, one of which involved failing to establish or maintain a CIP in violation of Rule 3310 that was appropriate for the firm's size and business.20 FINRA found that the member firm automatically approved accounts and ignored alerts despite the fact that its clearing firm had flagged those accounts as requiring further review for potentially fraudulent activity. The firm approved and opened more than 5.5 million new customer accounts during a two-and-a-half-year period without any employee whose primary responsibilities related to the firm's CIP, charged FINRA.

FINRA fined another member firm $650,000 for, among other things, allegedly failing to establish an AML compliance program reasonably designed to detect, monitor, and cause the reporting of potentially suspicious activity relating to low-priced securities transactions.21 FINRA found that the firm failed to monitor for potentially suspicious activity involving equity trading.

Even when the firm later implemented monitoring systems, the systems were not reasonably designed to detect red flags associated with low-priced securities transactions. In addition, the firm supposedly failed to provide appropriate guidance and direction to its employees on how to properly

use the systems, and ultimately did not detect and investigate several suspicious low-priced securities transactions.

FINRA fined another member firm $500,000 for, among other things, allegedly failing to describe in its AML policies "how the firm or its registered representatives should review or monitor customer stock deposits or subsequent trading activity to detect and investigate such red flags."22 Further, FINRA found that the firm's AML policies failed to describe and identify how the firm would investigate such red flags. In connection with the matter, FINRA also fined the firm's AML compliance officer $5,000, claiming the officer failed to properly implement the firm's AML policies and procedures.

Looking Ahead

In the past year, FINRA issued guidance and brought numerous enforcement actions in areas such as PFOF, market access, finfluencers and gamification, and AML. Many enforcement actions in the above high-priority and related topics resulted in heavy penalties and large fines for member firms, which serve as cautionary tales to industry participants of the perils and high costs of noncompliance.

As innovative technologies and business methodologies continue to emerge and challenge existing regulatory paradigms in 2022, member firms can expect further communications and enforcement actions. To that end, FINRA has stressed that it will "adapt its areas of focus throughout 2022 to address emerging regulatory concerns and risks for investors that may arise throughout the year,"23 including topics reviewed in this advisory as well as many others highlighted in FINRA's 2022 Report on Examination and Risk Monitoring Program, such as firm short positions and fails-t--receive in municipal securities; trusted contact persons; funding portals and crowdfunding offerings; disclosure of routing information; and portfolio margin and intraday trading.

Katten Muchin Rosenman LLP – Susan Light, Michael J. Lohnes and Alexander C. Kim

March 3 2022

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1 FINRA, "2022 Report on FINRA's Examination and Risk Monitoring Program" (Feb. 9, 2022), https://www.finra.org/rules-guidance/guidance/reports/2022-finras-examination-and-risk-monitoring-program.

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Aileen Tan, Financial Markets and Funds associate and candidate for admission to the New York State Bar, contributed to this advisory.

FINRA Issues 2022 Report on Its Examination and Risk Monitoring Program.

On February 9, 2022, the Financial Industry Regulatory Authority (FINRA) published its 2022 Report on its Examination and Risk Monitoring Program (the Report).1 The 60-page Report includes five new topic areas for 2022, flagged as such in the Report's table of contents: (1) firm short positions and fails-to-receive in municipal securities, (2) trusted contact persons, (3) funding portals and crowdfunding offerings, (4) disclosure of order routing information, and (5) portfolio margining and intraday trading.

FINRA highlights seven topic areas that received industry and public attention and were addressed through FINRA's exam and risk monitoring program: (1) Reg BI and Form CRS, (2) the Consolidated Audit Trail, (3) order handling, best execution, and conflicts of interest, (4) mobile apps, (5) special purpose acquisition companies (SPACs), (6) cybersecurity, and (7) complex products.

The Report also includes the perennial topic areas of past reports including anti-money-laundering, outside business activities, net capital, and books and records. The appendix includes specific examples of how firms have used prior FINRA reports and guidance to enhance their own compliance programs.

Sidley's Takeaways

While the Report covers more than 20 regulatory areas, some common themes emerge throughout.

First, the Report places a greater emphasis than past reports on topic areas in involving market integrity. This comes as no surprise given the volatility experienced in the markets during 2021. Firms should expect continued attention to best execution and compliance with the order routing disclosure requirements of Rule 606 of Regulation NMS. FINRA emphasizes wholesale market maker best execution obligations and notes that best execution is one of the "cornerstones" of FINRA's oversight activities. The Report informs us that FINRA, like the Securities and Exchange Commission, is focused on questions of potential conflicts of interest in payment for order flow arrangements with a clear shift in focus to firms with a zero-commission model. The findings from the 2020 targeted exam of zero-commission firms are still pending. Firms also should be prepared

for CAT reporting compliance to be front and center in examinations this year, particularly as the final phases of rollout are completed. FINRA already has identified particular areas of noncompliance.

Second, as the industry changes the ways in which it offers services, the Report suggests that FINRA is increasingly focusing attention on online platforms and digital communications through which newer investors are often opening brokerage accounts. The manner in which firms are communicating through mobile apps, social media, and other digital platforms all have drawn FINRA's attention and look to be in sharp focus in 2022. FINRA likely will look to hold communications on these platforms to the same standards of any other platform.

Last, but not least, 2022 will be the second full year of examinations for Reg BI compliance. As discussed below, firms should be prepared for examinations to include more substantive questions of Reg BI compliance in connection with specific recommendations such as private placements or complex products as well as examination of communications and whether they rise to the level of "recommendation," particularly in connection with online broker-dealer models.

The Report is intended to provide broker-dealers with information to use to prepare for examinations and to review and assess compliance and supervisory procedures related to business practices, compliance, and operations. It also is an important preview of areas that may garner the interest of FINRA Enforcement.

Key Report Highlights

We summarize some key highlights of the Report below.

Reg BI and Form CRS

The Report provides extensive feedback for firms on Reg BI and Form CRS compliance exam findings. In particular, FINRA flags concerns about firms failing to update written supervisory procedures to address these ne requirements, in particular in the areas of

- identifying the individual(s) responsible for Reg BI and Form CRS compliance
- providing adequate detail regarding how the firm is complying with new requirements
- addressing costs and potential alternatives in making recommendations
- addressing recommendations of account types
- addressing conflicts of interest and incentives
- including recordkeeping and testing requirements
- memorializing processes or controls developed to address Reg BI and Form CRS

FINRA also found that some firms had inadequate training, failed to comply with duty of care obligations, and failed to provide "full and fair" disclosure of material facts related to the scope and terms of the customer relationship. Form CRS filings that exceeded the prescribed page length, omitted material facts or otherwise contained inaccuracies or omissions, and were not properly posted on firm websites were among other specific Form CRS observations in the Report. Firms will want to review carefully this section and pay close attention as FINRA is looking beyond basic procedures compliance and will review the supervision of the marketing and recommendations of accounts and particular product types through the lens of Reg BI compliance.

Order Handling, Best Execution, and Conflicts of Interest

Compliance with FINRA's best execution rule, Rule 5310, is a perennial focus area for FINRA. This year the Report reinforced FINRA's focus on payment for order flow (PFOF) arrangements and

noted that it has been conducting a target review of wholesale market makers to evaluate their own execution quality reviews, whether PFOF arrangements influence their order handling practices, and any changes made in order handling practices during periods or market volatility. As the Report notes, FINRA examinations also found that some firms failed to assess execution in competing markets and failed to evaluate certain factors identified in Rule 5310 during "regular and rigorous reviews" such as speed of execution, price improvement, and the likelihood of execution of limit orders.

Consolidated Audit Trail (CAT)

According to the Report, CAT compliance is top of mind for FINRA. The Report identifies several findings of deficiencies including the submission of incorrect or incomplete reports. Exam findings also noted late resolution of repairable CAT errors and inadequate vendor supervision. As the final stages of the CAT rollout complete this summer, it will be important for broker-dealers to have effective supervisory procedures reasonably designed to achieve compliance with CAT reporting requirements that include using CAT report cards and considering a comparative review of CAT submissions against firm order records.

Mobile Apps

FINRA has increased its focus on educating newer investors entering the market through self-directed accounts and issued a special notice on June 30, 2021, requesting comments on effective ways to educate those new investors. The Report advises that firms using mobile apps must establish and implement a comprehensive supervisory system for communications on mobile apps so that statements are fair and balanced and do not contain false, misleading, or promissory statements. The Report also indicates that a false or misleading statement on one screen of a mobile app is not cured by a "one-click away" corrective disclosure. Given the Report's focus on mobile apps, expect FINRA to scrutinize all mobile app disclosures and communications in the same manner as any other written communication.

FINRA notes that firms using mobile apps to conduct business with their customers need to pay attention to whether information provided to customers via the app constitutes a "recommendation" that Reg BI would cover. Firms offering self-directed accounts will want to give particular attention to this issue.

Digital Communication Channels

FINRA advises firms to review policies on digital communications to address all permitted and prohibited communication channels and features. This comes on the heels of increased regulatory scrutiny in 2021 of record-retention practices for digital communications. FINRA also notes that firms should have processes to review for red flags of registered representatives' communication through unapproved digital channels and should review whether content on approved digital platforms, including social media, meets the standards of FINRA Rule 2210. For firms with mobile apps and other forms of digital communication, firms should be testing the accuracy of account and other information displayed in the mobile apps to confirm accuracy.

For those firms also engaged in digital asset activities, the Report notes that they should be confirming that there is a fair and balanced presentation addressing risks of digital assets and not misrepresenting the extent to which digital assets are regulated by FINRA or securities laws or eligible for SIPC or other protections thereunder.

Cybersecurity and Technology Governance

In 2021, mitigating the risk of online account takeovers and potential cyberintrusions through third-party vendors garnered FINRA's attention. FINRA observed that some firms did not have an adequate risk assessment process in place including failing to conduct regular penetration testing. Some firms also failed to encrypt all confidential data and sensitive firm information. Technology governance has been a key examination and enforcement focus for FINRA for some time. The Report shares key questions firms should consider in its technology governance, including what controls the firm implements to mitigate system capacity performance and integrity issues, how firms test system changes prior to being moved to a production environment, and postimplementation quality assurance. FINRA observed system capacity issues at firms during market volatility periods in 2021, and firms can expect that the regulator will remain watchful in this area throughout the next year.

Complex Products

Not surprisingly, the Report makes clear that FINRA will continue to look to risk disclosure and communications with customers about complex products. The Report turns particular focus to supervision and suitability of complex options strategies and approval for options trading. FINRA issued a regulatory notice on the topic, RN 21-15, in April 2021, followed by the launch of an ongoing targeted examination on options supervision and suitability in August 2021. The Report highlights conservation donation transactions as an area of concern as well as FINRA's longstanding interest in variable annuity transactions.

SPACs

SPACs make a reappearance in this year's Report where FINRA notes that over 70% of initial public offerings in the first quarter of 2021 were accomplished through SPACs. In October 2021, FINRA launched a targeted exam to explore a range of issues with SPACs including whether firms perform adequate due diligence on merger targets, whether adequate disclosures are provided to customers, and how firms are managing potential conflicts of interest in SPACs. FINRA will release its findings from this sweep at a later date.

The Report provides a thorough roadmap to FINRA's examination findings in key program areas. Firms should consider and implement, as necessary, practices and procedures in each of the areas and be prepared to address them in future examinations.

1 A copy of the complete Report is available at https://www.finra.org/rules-guidance/guidance/reports/2022-finras-examination-and-risk-monitoring-program.

Sidley Austin LLP – James Brigagliano, W. Hardy Callcott, Corin R. Swift, Lara C. Thyagarajan, Paul M. Tyrrell, Michael D. Wolk and Timothy B. Nagy

March 2, 2022

Firm Short Positions and Fails-to-Receive in Municipal Securities: 2022 Report on FINRA's Examination and Risk Monitoring Program

Regulatory Obligations and Related Considerations

Regulatory Obligations:

As detailed in *Regulatory Notice* 15-27, customers may receive taxable, substitute interest instead of

the tax-exempt interest they were expecting when a firm effects sales to customers of municipal securities that are not under the firm's possession or control.7 This can occur when firm trading activity inadvertently results in a short position or a firm fails to receive municipal securities it purchases to fulfill a customer's order.

Firms must develop and implement adequate controls and procedures for detecting, resolving and preventing these adverse tax consequences to customers. Such procedures must include closing out fails-to-receive within the time frame prescribed within Municipal Securities Rulemaking Board (MSRB) Rule G-12(h) and confirming that their communications with customers regarding the tax status of paid or accrued interest for municipal securities are neither false nor misleading, in accordance with MSRB Rule G-17.

Related Considerations:

- Does your firm use exception reports to manage its municipal securities' short positions or fails-t--receive? If so, how does your firm use such reports, and which departments are responsible for managing them?
- When municipal securities short positions are identified, does your firm begin to cover the shorts, or do they wait until the trades have settled?
- What is your firm's process to close out fails-to-receive in accordance with the methods and time frame prescribed under MSRB G-12(h)?
- How does your firm detect instances that would require them to pay customers substitute interest? In those circumstances, what is the firm's process for notifying impacted customers and paying them substitute interest in a timely manner? If a customer does not want to receive substitute interest, what alternatives does the firm offer (e.g., offering to cancel the transaction and purchasing a comparable security that would provide tax-exempt interest)?
- How does your firm handle inbound or outbound account transfers sent through the Automated Customer Account Transfer Service (ACAT) that are delivered with no corresponding municipal bonds in possession or control?

Exam Findings and Effective Practices

Exam Findings:

- **Inadequate Controls and Procedures** – Not maintaining adequate procedures and controls for preventing, identifying and resolving adverse consequences to customers when a firm does not maintain possession or control of municipal securities that a customer owns.
- **Inadequate Lottery Systems** – Opting to use a random lottery system to allocate municipal short positions to certain customer accounts, but the system did not fairly or adequately account for or allocate substitute accrued interest payments.

Effective Practices:

- **Preventative Controls** – Maintaining processes to prevent or timely remediate municipal positions from settling short (e.g., covering these positions, finding a suitable alternative, cancelling the customer's purchase).
- **Operational and Supervisory Reports** – Developing operational and supervisory reports to identify customer long positions for which the firm has not taken possession and control of the security.
- **Review of Fail Reports** – Municipal securities principals performing regular, periodic reviews of Fail Reports to comply with the close-out requirements of MSRB Rule G12-(h).

Additional Resource

Regulatory Notice 15-27 (Guidance Relating to Firm Short Positions and Fails-to-Receive in Municipal Securities)

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7 These regulatory obligations stem from Exchange Act Rule 15c3-3(d)(4) and MSRB Rules G-17 and G-27 (for firm shorts), and MSRB Rule G12-(h) (for fails-to-receive).

California Warns Investors of Labor Market and Supply Chain Issues.

California, whose recovery of jobs lost during the height of the pandemic lags that of the U.S. overall, said low labor market force growth and supply chain disruptions pose risks to its municipal-bond investors.

In documents circulated to potential buyers of its $2.2 billion general-obligation deal on March 9, the state added the threats to its list of dangers they should consider.

The administration of Governor Gavin Newsom expects the labor force to recover to pre-pandemic levels in the third quarter this year. “If current labor market frictions (impediments to employers and job seekers agreeing on employment, e.g., disagreements on appropriate wages, workplace safety or ability to work remotely) persist longer than projected, then low labor force growth would constrain job growth, which in turn would lead to less consumption and spending,” the state said in the documents.

California has regained 72% of the jobs lost during the onset of the pandemic, while the nation has recovered 87%, according to federal data. Its unemployment rate of 6.5% in December was the highest among U.S. states.

Meanwhile, the pandemic-wreaked havoc at factories and ports also present a threat to the state. If regular production and transportation don’t resume by early 2023 as expected by the administration, “a slower resolution of supply chain issues would potentially keep inflation high for longer than assumed and could also lead to lower production and economic activity,” the state said.

In the bond documents, California listed 13 risks. They are:

- Covid-19 pandemic
- Threat of recession
- Inflation
- Labor market friction
- Supply chain disruptions
- Capital gains volatility
- Global relations and trade
- Health care costs
- Housing constraints
- Debts and liabilities
- Climate change
- Energy risks
- Cybersecurity risks

California's general obligation bonds are rated Aa2 by Moody's Investors Service, AA- by S&P Global Ratings and AA by Fitch.

Bloomberg Markets

By Romy Varghese

March 2, 2022

Post-Issuance Tax Compliance and Continuing Disclosure Responsibilities for Issuers and Borrowers of Tax-Exempt Bonds (Second Edition) - Orrick

The tax-exempt bond market is perennially under heightened scrutiny by various regulators, including the Internal Revenue Service (the "IRS"), the United States Securities and Exchange Commission (the "SEC") and the Municipal Securities Rulemaking Board (the "MSRB"). A primary focus of these regulators is on post-issuance compliance.

The purpose of this publication is to summarize the topic of post-issuance compliance for interested parties. It is intended to assist:

- treasurers, finance directors, comptrollers, controllers and other responsible officials of state and local government issuers of tax exempt bonds ("Issuers"); and
- representatives of private, nongovernmental conduit borrowers (such as nonprofit institutions providing health care and higher education) that are allowed to borrow at tax-exempt rates from Issuers ("Borrowers").

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Orrick, Herrington & Sutcliffe LLP

February 23, 2022

FINRA Report Highlights New Topics and Emerging Risks for 2022.

On February 9, FINRA published its 2022 Report on FINRA's Examination and Risk Management Program (2022 Report), an authoritative resource for member firms to evaluate and, where necessary, enhance their compliance programs and operations procedures. The 2022 Report is just the second iteration of FINRA's pathbreaking annual Report on FINRA's Examination and Risk Management Program, which FINRA describes as an "up-to-date, evolving resource or library of information for firms." The annual report outlines relevant rule(s), key considerations, noteworthy findings, and effective practices on a broad range of regulatory obligations organized into four categories: (1) firm operations, (2) communications and sales, (3) market integrity, and (4) financial management.

The first report (2021 Report) synthesized and supplanted two of FINRA's prior annual publications, bringing together (1) FINRA's analysis of prior examination results, historically provided in the Report on Examination Findings and Observations; and (2) FINRA's forward-looking Risk Monitoring

and Examination Program Priorities Letter, which highlighted the issues on which FINRA planned to focus its reviews for the coming year. Building upon the content of the 2021 Report (which we previously covered here), the 60-page 2022 Report includes several new topics, and identifies key areas of emerging risk that may receive increased scrutiny going forward. The 2022 Report also highlights several topics that received significant industry and public attention in 2021, including: (1) new SEC rules, such as Regulation Best Interest and Form CRS; (2) the increasing prevalence and sophistication of cybersecurity attacks; (3) securities trading via mobile applications; and (4) the increased use of special purpose acquisition companies (SPACs) to bring companies public. The 2022 Report states that FINRA will continue to assess member firms' programs and share information on these topics of interest as they develop, including in future annual reports.

Below, we summarize five entirely new topics found in the 2022 Report and catalog the emerging risks that FINRA has identified as likely to receive increased scrutiny in 2022 and beyond. However, FINRA member firms are encouraged to thoroughly review the 2022 Report. In particular, member firms should: (1) pay close attention to the topics that FINRA has flagged as "new" to the 2022 Report; and (2) identify the findings, observations, and effective practices relevant to their business models. The findings and best practices outlined in the 2022 Report can serve as a guide for member firms to evaluate their compliance programs and operations procedures to identify possible deficiencies or gaps that could result in the types of exam findings highlighted therein. The 2022 Report also may serve as a road map to prepare for an examination. If concerns arise before an examination, member firms would be well served by including counsel familiar with these issues in their preparation for the examination.

I. New Topics Covered in the Report

Firm Short Positions and Fails-to-Receive in Municipal Securities. Customers may receive taxable, substitute interest instead of the expected tax-exempt interest when a firm effects sales to customers of municipal securities not under the firm's control — for example, when firm trading activity inadvertently results in a short position or when a firm fails to receive municipal securities it purchased to fulfill a customer's order. Firms must develop and implement adequate controls and procedures for detecting, resolving, and preventing these adverse tax consequences to customers.

Trusted Contact Persons. FINRA Rule 4512(a)(1)(F) requires firms, for each of their noninstitutional customer accounts, to make a reasonable effort to obtain the name and contact information for a trusted contact person age 18 or older, and describes the circumstances in which firms are authorized to contact the trusted contact person and disclose information about the customer account.

Funding Portals and Crowdfunding Offerings. Funding portals must register with the SEC and become a member of FINRA. Broker-dealers contemplating engaging in the sale of securities in reliance on the crowdfunding exemptions must notify FINRA in accordance with FINRA Rule 4518.

Disclosure of Routing Information. Rule 6060 of Regulation NMS requires broker-dealers to disclose information regarding the handling of their customers' orders in NMS stocks and listed options, so that customers can (1) better understand how the firm routes and handles their orders, (2) assess the quality of order handling services, and (3) ascertain whether the firm is effectively managing potential conflicts of interest.

Portfolio Margin and Intraday Trading. FINRA Rule 4210 permits member firms to apply portfolio margin requirements in margin accounts held by certain investors as an alternative to strategy-based margin requirements. Firms are required to monitor the risk of the positions held in these accounts during a specified range of possible market movements according to a

comprehensive written risk methodology.

II. Emerging Risks

Emerging Low-Priced Securities Risk. FINRA has observed an increase in several types of activity in low-priced securities that could be indicative of fraud schemes, including an increase in such activity through foreign financial institutions that open omnibus accounts at U.S. broker-dealers.

Emerging Vendor Risk. Due to the recent increase in the number and sophistication of cyberattacks during the COVID-19 pandemic, FINRA reminds firms of their obligations to oversee, monitor, and supervise cybersecurity programs and controls provided by third-party vendors.

Emerging Customer Account Information Risks. Effective February 15, 2021, FINRA Rule 3241 requires a registered person to decline being named a beneficiary of a customer's estate, executor, or trustee or to have power of attorney for a customer unless certain conditions are met, due to the risk of a conflict of interest. Among other things, firms should (1) consider whether their policies and procedures establish criteria for a registered person acting in such capacity and (2) be able to perform a reasonable assessment of the risks of a registered person in such a position.

FINRA member firms should thoroughly review the 2022 Report, including the areas highlighted above, to identify the findings, observations, and effective practices relevant to their business models, and they should incorporate relevant practices into existing compliance programs.

Troutman Pepper – Jay A. Dubow, Ghillaine A. Reid, Bonnie Gill and Casselle Smith

February 17 2022

FINRA Publishes 2022 Report on Its Examination and Risk Monitoring Program: Mayer Brown

On February 9, 2022, the Financial Industry Regulatory Authority, Inc. ("FINRA") published its 2022 Report on FINRA's Examination and Risk Monitoring Program (the "Report"). FINRA intends for the Report to be an up-to-date, evolving resource for firms that may help inform their compliance programs. In this regard, the Report builds on the structure and content of last year's report and adds new topics for 2022, including funding portals and crowdfunding offerings, trusted contact persons, disclosure of routing information, portfolio margin and intraday trading, and firm short positions and fails-to-receive in municipal securities, as well as new material, such as new exam findings and effective practices, to topics that FINRA covered in 2021. Further, for each topical area covered in the Report, FINRA provides the relevant rule(s), key considerations for member firms' compliance programs, noteworthy findings from recent examinations, including findings that are particularly relevant for new member firms in their first year of operation, effective practices that FINRA observed during its oversight, and additional resources that may be helpful to member firms in reviewing their supervisory procedures and controls and fulfilling their compliance obligations. Firms should carefully review the Report as applicable to their business operations with a view to identifying potential gaps and/or areas for enhancement in their compliance programs and supervisory controls. In addition to the new topics for 2022, firms should pay attention to the new material that FINRA added to previously covered topics, in particular new exam findings and effective practices. When preparing for upcoming exams, firms should ensure that they can explain

their current practices and that their current practices are appropriately documented, including relevant supervisory reviews, compliance reports and testing of supervisory systems.

Selected Highlights

The Report highlights certain areas that received considerable attention within the industry and beyond in 2021.

Regulation Best Interest ("Reg BI") and Form CRS. Firms should continue to expect FINRA to undertake a comprehensive review of firms' processes, practices and conduct in relation to requirements under Reg BI and Form CRS, including whether firms have established and enforce adequate written supervisory procedures ("WSPs"), file, deliver and track accurate Forms CRS, make recommendations that adhere with Reg BI's Care Obligation, identify and mitigate conflicts of interest and provide effective staff training.

Consolidated Audit Trail ("CAT"). FINRA continues to evaluate member firms for compliance with obligations under Rule 613 under the Securities Exchange Act of 1934 (the "Exchange Act") and the CAT NMS Plan FINRA Rule 6800 Series (collectively, the "CAT Rules"). FINRA emphasizes several aspects of the CAT Rules, including reporting required information to the Central Repository and maintaining effective supervision processes.

Order Handling, Best Execution and Conflicts of Interest. FINRA emphasizes that assessing firms' compliance with their best execution obligations under FINRA Rule 5310 (Best Execution and Interpositioning) is one of the cornerstones of FINRA's oversight activities and that it has evolved its oversight program to address changes in firms' business models, such as the advent of the "zero commission" model. FINRA launched a targeted exam initiative to evaluate the impact of the zero commission model on firms' order-routing and other business practices.1 FINRA also is reviewing firms' order handling disclosures for compliance with the requirements of SEC Rule 606 of Regulation NMS.

Mobile Apps. FINRA points out that the use of mobile applications ("apps") and related technologies to attract and interact with customers raise novel questions and potential concerns, including whether they encourage retail investors to engage in trading activities and strategies that may not be consistent with their investment goals or risk tolerance and how the apps' interface designs could influence investor behavior. FINRA notes that it has identified significant problems with some mobile apps' communications with customers and firms' supervision of activity on those apps, particularly controls around account openings. FINRA also launched a targeted exam initiative to assess firms' use of social media to acquire customers and compliance with obligations relating to the collection of information from those customers and other individuals who may provide data to firms.2

Special Purpose Acquisition Companies ("SPACs"). FINRA has increased its focus on firms' compliance with regulatory obligations in executing SPAC transactions. FINRA identifies several focus areas in its review of firms participating in SPAC offerings, including: due diligence conducted at the IPO and business combination stages, including as to the relevant officers, directors and control persons of the SPAC and SPAC-sponsor(s) and pre-identified acquisition targets; compliance with FINRA rules governing outside business activities ("OBAs"), private securities transactions ("PSTs") and Form U-4 amendments for associated persons who hold positions with, advise or personally invest in, SPACs or SPAC sponsors; whether firms are correctly taking net capital charges relative to the size of their commitment or using a written agreement with another syndicate member (i.e., "backstop provider"); and whether firms are maintaining and regularly updating their WSPs and supervisory controls to address risks related to SPACs (e.g., Reg BI, due diligence,

information barrier policies, conflicts of interest). FINRA launched a targeted exam to explore issues relating to firms' SPAC activities, including how firms manage potential conflicts of interest in SPACs, whether firms are performing adequate due diligence on business combination targets and if firms are providing adequate disclosures to customers.3

On a separate note, FINRA advises firms that underwrite IPOs of issuers based in the People's Republic of China ("China-based issuers") to evaluate carefully whether the firms' controls are able to identify and report market manipulation, other abusive trading practices and potential anti-money laundering ("AML") concerns, which may result from the involvement of nominees for an undisclosed control person. In this respect, FINRA describes numerous red flags of potentially manipulative trading associated with how these investors open new accounts and trade these securities after completion of the IPO. FINRA also provides a list of resources regarding the risks associated with China-based issuers in recent statements from the U.S Securities and Exchange Commission ("SEC"). For additional information regarding the risks associated with China-based issuers, see our previous article here.

Cybersecurity. FINRA describes cybersecurity threats as "one of the primary risks firms and their customers face." In 2021, FINRA observed a continued increase in the number and sophistication of these threats and has issued alerts about phishing campaigns involving fraudulent emails purporting to be from FINRA, new customers opening online brokerage accounts to engage in Automated Clearing House ("ACH") "instant funds" abuse, the increase in bad actors using compromised registered representative or employee email accounts to execute transactions or move money, the use of customer information to gain unauthorized entry to customers' email accounts, online brokerage accounts or both (i.e., customer account takeover incidents), and using synthetic identities to fraudulently open new accounts.4 FINRA will continue to assess firms' information security programs and share information about cybersecurity threats and effective practices.

Complex Products. FINRA will continue to review firms' communications and disclosures made to customers in relation to complex products. FINRA will review customer account activity to assess whether firms' recommendations regarding these products are in the best interest of retail customers given their investment profile and the potential risks, rewards and costs associated with the recommendation. FINRA launched a targeted exam initiative in August 2021 to review firms' practices and controls relating to the opening of options accounts, which in some cases may be used to engage in complex investment strategies.5 With respect to mitigating the risk that recommendations of high-risk or complex investments might not be in a retail customer's best interest, FINRA notes as an effective practice establishing product review processes to identify and categorize risk and complexity levels for existing and new products, limiting high-risk or complex product, transaction or strategy recommendations to specific customer types, and applying heightened supervision to recommendations of high-risk or complex products.

Core Topics

The Report addresses 21 regulatory areas organized into four categories: Firm Operations; Communications and Sales; Market Integrity; and Financial Management. We highlight below the new topics for 2022 and the new material that FINRA added to previously covered topics.

FIRM OPERATIONS

The Firm Operations section of the Report discusses AML obligations, cybersecurity and technology governance, OBAs and PSTs, books and records, regulatory events reporting under FINRA Rule 4530, firm short positions and fails-to-receive in municipal securities, trusted contact persons and funding portals and crowdfunding offerings.

FINRA highlights several considerations relating to both AML and cybersecurity and technology governance. FINRA notes that firms experiencing substantial growth or changes to their business should provide for reasonable growth and evolution in their AML programs alongside the business. In our experience, FINRA takes a similar view with respect to firms' cybersecurity and technology governance programs. FINRA also indicates that firms should consider whether they have appropriate procedures to communicate cyber events to their AML department, Compliance department or both, to fulfill regulatory obligations such as the filing of suspicious activity reports (" SARs"). In this regard, FINRA highlights as an exam finding that firms did not notify their AML departments of events that involve suspicious transactions including cybersecurity events, account compromises or takeovers, new account fraud, fraudulent wires and ACH transfers.6 FINRA expects that events involving, or enabled by, cybercrime be reported via SARs. In addition, FINRA urges firms to consider how FinCEN's 2021 publication of government-wide priorities for AML and countering the financing of terrorism will be incorporated into their risk-based AML programs.

FINRA addresses risks relating to OBAs and PSTs and reminds firms of their obligation under FINRA Rule 3270.01 to determine whether proposed OBAs will interfere with or otherwise compromise the registered representative's responsibilities to the firm and its customers, or should be treated as a PST subject to the requirements of FINRA Rule 3280. FINRA highlights as an effective practice conducting due diligence of OBAs that involve raising capital or directing securities transactions with investment advisers or fund companies in order to identify potential PSTs.

FINRA emphasizes, in particular for new member firms, that for purposes of compliance with the books and records requirements under SEC Rules 17a-3 and 17a-47 and FINRA rules, firms must file a Financial Notification when selecting or changing an archival service provider. Firms also should perform due diligence to verify vendors' ability to comply with applicable books and records requirements, including standards for electronic storage media ("ESM") and ESM notification requirements, and confirm that service contracts and agreements comply with ESM notification requirements. FINRA found that firms failed to comply with the ESM notification requirements, such as not obtaining the third-party attestation letters required by SEC Rule 17a-4(f)(3)(vii). FINRA also highlights as an effective practice firms' review of vendor contracts and agreements to assess whether firms will be able to comply with applicable books and records requirements.

FINRA did not add any new content with respect to regulatory events reporting under FINRA Rule 4530, but the Report's discussion of exam findings and effective practices in this area serves as helpful guidance.

With respect to firm short positions and fails-to-receive in municipal securities, a new topic in 2022, FINRA highlights findings relating to inadequate controls and procedures for preventing, identifying and resolving adverse consequences to customers when a firm does not maintain possession or control of municipal securities, which may result in customers receiving taxable, substitute interest instead of tax-exempt interest as expected. FINRA suggests certain effective practices to identify and prevent this issue, including developing operational and supervisory reports to identify customer long positions for which the firm has not taken possession or control of the security.

Another new topic in 2022 is trusted contact persons ("TCP"), as defined in FINRA Rule 4512(a)(1)(F). FINRA notes exam findings relating to firms' failure to make a reasonable attempt to obtain the name and contact information of a TCP for all non-institutional customers and not providing certain TCP-related written disclosures. FINRA also notes emerging customer account information risks relating to when registered representatives are named a beneficiary of a customer's estate, executor or trustee, or have a power of attorney for a customer.

FINRA adds discussion of regulatory obligations related to funding portals and crowdfunding

offerings as a new topic in 2022. This is consistent with the increased SEC enforcement focus on crowdfunding. In September 2021, for example, in its first action in this area, the SEC charged a registered funding portal and certain of its executives in connection with allegedly conducting fraudulent and unregistered crowdfunding offerings. The Report identifies a number of exam findings, including among these, missing disclosures. Offerings on platforms have failed to include disclosures required by Regulation Crowdfunding, such as use of proceeds descriptions, offering process details, descriptions of capital stock, and financial statements. Funding portals also are failing to report written customer complaints (required by FINRA Funding Portal Rule 300(c)) and failing to make required filings, such as statements of gross revenues, within the specified time periods. The Report suggests developing annual compliance questionnaires to, among other things, verify the accuracy of associated persons' disclosures, as well as developing compliance checklists and schedules in order to assist in the process of confirming that obligations are being met in a timely manner. In addition, the Report notes that funding portals should be implementing supervisory review procedures tailored to the communications requirements applicable to portals.

COMMUNICATIONS AND SALES

The Communications and Sales section of the Report discusses Reg BI and Form CRS, communications with the public, private placements and variable annuities.

The Report contains a substantial amount of new material relating to Reg BI and Form CRS, including an overview of key regulatory considerations, a list of exam findings and a summary of effective practices observed in connection with FINRA's oversight activities. FINRA notes that the findings present an initial look at firms' practices and, as it continues to conduct exams and gather additional information on firms' practices, FINRA intends to publish additional findings in the future.

In addition, the Report includes a substantial amount of new content relating to communications with the public, with a particular focus on communications relating to mobile apps, digital assets, cash management accounts and municipal securities. For example, FINRA highlights findings relating to false, misleading and inaccurate information in mobile apps, including providing incorrect account balance or historical performance information, sending margin call warnings to customers whose account balances were not approaching or were below minimum maintenance requirements, and distributing false and misleading promotions through social media and "push" notifications that made promissory claims or omitted material information. FINRA also highlights several considerations for communications relating to municipal securities. FINRA reminds new member firms that they are required to file, prior to use, retail communications that are published or used in any electronic or other public media with FINRA's Advertising Regulation Department during their first year of membership.8 FINRA notes that it has observed deficient communications promoting digital assets that may create confusion about the role of the broker-dealer in relation to other entities involved in the offer of digital assets.

Given the increased reliance by issuers on private placements, the Report once again includes a discussion of private placements. The Report reminds firms of their due diligence obligations in connection with private placements, which are set forth in FINRA RN 10-22. The Report notes that FINRA's suitability rule continues to apply to non-retail customers, and Reg BI applies to recommendations to retail customers of any securities transaction, including recommendations relating to a private placement. The Report reminds firms of their obligation to make timely filings under FINRA Rules 5122 or 5123, and reminds firms of the recent amendments to these rules.9 Among its findings, FINRA notes that some firms failed to perform reasonable diligence concerning private placements, especially in connection with offerings that relate to issuers in businesses as to which the member firm lacks specialized experience. In addition, FINRA notes it has observed in exams that firms failed to inquire into and analyze red flags identified during the diligence practice.

The Report highlights a number of effective practices in the area, including: creating checklists relating to private placements; conducting and documenting independent research on offerings and addressing any identified red flags; independently verifying aspects of the business plan that are key to the future prospects; identifying and addressing any conflicts of interest; and post-offering, conducting a review to ascertain whether offering proceeds were used in a manner consistent with the plan disclosed in the offering materials.

FINRA addresses risks relating to variable annuities in new content regarding firms' processes to supervise registered representatives who advise their clients' decisions on whether to accept a buyout offer. FINRA highlights findings relating to poor and insufficient data quality on variable annuity transactions, particularly in connection with exchange transactions, as well as failing to address inconsistencies in available data for variable annuities, data formats and reporting processes. FINRA notes as an effective practice creating automated solutions to synthesize variable annuity data when warranted in light of transaction volumes.

MARKET INTEGRITY

The Market Integrity section of the Report discusses CAT reporting obligations, best execution, disclosure of routing information, and the market access rule.

FINRA highlights several new exam findings relating to CAT reporting obligations, including inaccurate reporting of required information to the Central Repository, failure to resolve repairable CAT errors in a timely manner, and inadequate supervisory procedures and controls regarding CAT reporting and clock synchronization that are performed by third-party vendors.

FINRA emphasizes that best execution obligations apply to any firm that receives customer orders for purposes of handling and execution and reminds that any firm subject to FINRA Rule 5310 cannot transfer its duty of best execution to another person. FINRA urges firms to consider how they address potential conflicts of interest in order routing decisions, such as those involving affiliated broker-dealers or other entities, market centers that provide payment for order flow ("PFOF") or other orderrouting inducements, and orders received from customers of another broker-dealer for which the receiving firm provides PFOF. FINRA is conducting targeted best execution reviews of wholesale market makers concerning their relationships with broker-dealers that route to them as well as their own order routing practices and decisions.

Disclosure of routing information is a new topic for 2022. FINRA highlights numerous findings relating to order routing disclosures under Rule 606 of Regulation NMS, such as inaccurate quarterly reports (e.g., incorrectly stating that the firm does not have a profit-sharing arrangement or receive PFOF from execution venues), failure to adequately describe material aspects of the firm's relationships with disclosed venues in the quarterly report, and insufficient WSPs relating to, for example, failing to make updates to include new requirements of amended Rule 606(a)(1) or new Rule 606(b)(3).

FINRA adds new content regarding the Market Access Rule (SEC Rule 15c3-5). In particular, FINRA notes that the rule applies generally to securities traded on an exchange or alternative trading system ("ATS"), including equities, equity options, exchange-traded funds, debt securities, security-based swaps, security futures products and digital assets that meet the SEC's definition of a security. With respect to firms that operate an ATS that has subscribers that are not broker-dealers, FINRA instructs that such firms should consider how they establish, document and maintain a system of controls and supervisory procedures reasonably designed to manage the financial, regulatory and other risks of this business activity.

FINANCIAL MANAGEMENT

The Financial Management section of the Report discusses net capital, liquidity risk management, credit risk management, segregation of assets and customer protection, and portfolio margin and intraday trading.

With respect to net capital compliance, FINRA highlights, in particular for new member firms, that if firms have an affiliate paying any of their expenses, Notice to Members 03-63 of the former National Association of Securities Dealers, Inc. ("NASD") sets forth specific requirements for establishing an Expense Sharing Agreement. In addition, firms with office leases should apply the guidance in RN 1908 for reporting lease assets and lease liabilities on their FOCUS reports. Moreover, firms must align their revenue recognition practices with the requirements of the Financial Accounting Standards Board's Topic 606 (Revenue from Contracts with Customers).10

FINRA recently adopted a new filing requirement relating to firms' liquidity risk management practices for firms with large customer and counterparty exposures.11 The new requirement, the Supplemental Liquidity Schedule ("SLS"), becomes effective on March 1, 2022, and the first SLS, which will be filed as a supplement to the FOCUS report, is due by May 4, 2022. FINRA directs firms to consider whether their liquidity risk management practices include processes for accessing liquidity during common stress conditions and "black swan" events, determining how the funding would be used, and using empirical data from recent stress events to increase the robustness of firms' stress testing. FINRA states that it observed firms incorrectly basing clearing deposit requirements on information that does not accurately represent their business operations, such as using the amounts listed on FOCUS reports rather than spokes in deposit requirements that may have occurred on an intra-month basis. In addition, an effective practice, FINRA states that firms' liquidity management plans should consider material changes in market value of firm inventory over a short period of time.

FINRA includes credit risk management and segregation of assets and customer protection as topics in the Report, as it did in last year's Report, although neither section contains new content for 2022. Nevertheless, FINRA's discussion of considerations and exam findings relating to these topics should be reviewed carefully, including FINRA's discussion of digital assets in the context of SEC Rule 15c3-3.

With respect to portfolio margin and intraday trading, a new topic for 2022, FINRA highlights findings relating to systems that are not adequately designed to identify credit risk exposure on an intra-day and end-of-day basis, failure to promptly identify and escalate elevated risk exposures to senior management (in part due to insufficient expertise), and WSPs that do not adequately outline intraday monitoring processes and controls. FINRA identifies several effective practices relating to internal risk frameworks, concentration risk and communicating with clients with large or significantly increasing exposures.

CONCLUSION

The Report addresses a variety of topics, ranging from findings that FINRA highlighted in prior reports and that FINRA continues to note in recent examinations to emerging risks representing potentially concerning practices that FINRA has observed and which may receive increased scrutiny going forward. Firms should address potential gaps in their compliance programs and incorporate relevant practices in a manner tailored to their business operations.

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1 See FINRA Targeted Examination Letter on Zero Commissions (February 2020). FINRA intends to share findings in the future.

2 See FINRA Targeted Examination Letter on Social Media Influencers, Customer Acquisition, and Related Information Protection (September 2021). FINRA intends to share findings in the future.

3 See FINRA Targeted Exam Letter on Special Purpose Acquisition Companies ("SPACs") (October 2021). FINRA intends to share findings in the future.

4 See e.g., FINRA Regulatory Notice ("RN") 21-20 (FINRA Alerts Firms to Phishing Email Using "gateway-finra.org" Domain Name) (June 2021); FINRA RN 21-18 (FINRA Shares Practices Firms Use to Protect Customers From Online Account Takeover Attempts) (May 2021); and FINRA RN 21-14 (FINRA Alerts Firms to Recent Increase in ACH "Instant Funds" Abuse) (March 2021).

5 See FINRA Targeted Examination Letter on Option Account Opening, Supervision and Related Areas (August 2021). FINRA intends to share findings in the future.

6 FINRA also highlights certain considerations relating to emerging low-priced securities risk as well as emerging vendor risk for cybersecurity.

7 We note that the SEC has proposed amendments to SEC Rule 17a-4 to, among other things, allow for electronic records to be preserved in a manner that permits the recreation of an original record if it is altered, over-written, or erased. See Electronic Recordkeeping Requirements for Broker-Dealers, Security-Based Swap Dealers, and Major Security-Based Swap Participants, 86 Fed. Reg. 68300 (Dec. 1, 2021).

8 See FINRA Rule 2210(c)(1)(A). Note, however, that firms may seek a waiver from this requirement under FINRA Rule 2210(c)(9)(A).

9 See FINRA RN 21-26 (FINRA Amends Rules 5122 and 5123 Filing Requirements to Include Retail Communications That Promote or Recommend Private Placements) (July 2021) and FINRA RN 21-10 FINRA (Updates Private Placement Filer Form Pursuant to FINRA Rules 5122 and 5123) (March 2021). 10 See NASD Notice to Members 03-63 (SEC Issues Guidance on the Recording of Expenses and Liabilities by Broker/Dealers) (October 2003); see also FINRA RN 19-08 (Guidance on FOCUS Reporting for Operating Leases) (March 2019). 11 See FINRA RN 21-31 (FINRA Establishes New Supplemental Liquidity Schedule (SLS)) (September 2021).

Mayer Brown – Steffen Hemmerich, Anna T. Pinedo and Stephen Vogt

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FINRA's 2022 Report on Exam and Risk Monitoring Program Adds Five Topic Areas: Cadwalader

In its annual Examination and Risk Monitoring Program Report, FINRA covered twenty-one different topics related to a firm's core compliance responsibilities. FINRA added five new topics since last year's report. The new topic areas include:

- Firm Short Positions and Fails-to-Receive in Municipal Securities;
- Trusted Contact Persons;
- Funding Portals and Crowdfunding Offerings;
- Disclosure of Routing Information; and
- Portfolio Margin and Intraday Trading.

For covered topics, the Report (i) identifies the relevant rules, key considerations for member firms' compliance programs, and noteworthy findings from recent examinations, and (ii) outlines effective practices that FINRA observed during its oversight while providing resources that the member firms may find helpful when reviewing their procedures and fulfilling their compliance obligations. Some of the areas of focus highlighted in the Report were:

- "FINRA's initial findings from Reg BI and Form CRS reviews;
- firms' compliance with certain regulatory obligations related to:
- the Consolidated Audit Trail,
- best execution and
- Rule 606 of Regulation NMS;

- problems with some mobile apps' communications with customers and firms' supervision of activity on those apps, particularly controls around account openings;
- firms' compliance with their regulatory obligations with securities activities involving Special Purpose Acquisition Companies;
- the increasing number and sophistication of cybersecurity threats faced by firms and their customers; and
- firms' communications and disclosures made to customers regarding complex products."

FINRA stated that the Report is intended to be an up-to-date, evolving resource or library of information for firms.

Cadwalader Wickersham & Taft LLP

February 10 2022

FINRA Report Finds Short Position Controls Lacking.

Financial Industry Regulatory Authority examinations have uncovered a theme of inadequate controls and procedures related to municipal short positions and fails-to-receive, something the regulator stressed firms must be diligent about detecting and resolving to prevent adverse tax consequences to customers.

Firm short positions and fails-to-receive in municipal securities were among several new topics highlighted in the Financial Industry Regulatory Authority's 2022 report on its Examination and Risk Monitoring Program released Wednesday.

The 70-page report covers more than two dozen topics. In addition to other compliance areas, the report also provides exam findings and compliance recommendations regarding municipal securities advertisements and communications.

In a release, Greg Ruppert, FINRA's executive vice president for member supervision, noted the evolving nature of the securities industry landscape, describing it as "highly dynamic in terms of business models, technologies, products and compliance practices."

"FINRA's report looks at those significant changes through the lens of FINRA's commitment to investor protection and market integrity, so that firms' compliance programs can benefit from our findings about emerging and ongoing issues," Ruppert added.

In terms of content, for each of the compliance areas addressed, FINRA's report identified relevant rules and highlighted key compliance considerations.

"The report also summarizes noteworthy findings from recent examinations, outlines effective practices that FINRA observed during its oversight, and provides additional resources that may be helpful to member firms in reviewing their supervisory procedures and controls and fulfilling their compliance obligations," according to FINRA.

The section of the report dealing with regulatory obligations and considerations tied to firm short positions and fails-to-receive focused heavily on controls.

A muni short position, which FINRA has said in previous guidance is usually inadvertent, occurs

when a firm sells bonds it does not actually have. This is sometimes due to a failure to receive bonds it ordered, and it then has to make substitute payments on those securities to the customer. That substitute interest paid to the customer might actually be taxable, because the Internal Revenue Service will not allow both that customer and whoever actually holds the bonds to both receive tax-exempt interest.

FINRA has brought enforcement actions against firms related to this problem. Notably, Merrill Lynch agreed last year to pay more than $1 million to settle FINRA charges related to short positions.

In this report, FINRA noted that firms must "develop and implement adequate controls and procedures for detecting, resolving and preventing adverse tax consequences to customers" that can stem from sales of municipal securities that are not under a firm's possession or control.

FINRA pointed out that those procedures must include closing out fails-to-receive within time frames specified in the Municipal Securities Rulemaking Board's Rule G-12(h). Related communications must not be false or misleading as prescribed in MSRB Rule G-17.

Exam findings in this area showed inadequate controls and procedures in instances where a firm does not maintain possession or control of a customer's municipal securities.

FINRA also found lottery systems that it says, "do not fairly or adequately account for or allocate substitute accrued interest payments for allocating municipal short positions to certain customer accounts."

According to the report, some effective compliance practices for firm short positions and fails-t--receive include maintaining processes to prevent or remediate municipal positions from settling short, and developing operational and supervisory reports to identify customer long positions outside of the firm?s possession and control.

Conducting regular and periodic review of fail reports to ensure compliance with MSRB Rule G- 12(h), is another best practice, according to FINRA.

FINRA also posed a number of questions as related considerations in the municipal securities area. For example, does a firm use exception reports to manage municipal securities short positions or fails to receive? Another question involves timing – when municipal securities short positions are identified, does a firm cover the short or wait until the trades have settled?

Other considerations include the nature of a firm's process to close out fails-to-receive under MSRB Rule G-12(h), how firms detect instances that require them to pay customers substitute interest, and how firms handle inbound or outbound account transfers that are delivered without corresponding municipal bonds in possession or control.

The report also contains a section addressing regulatory obligations stemming from communications with the public, including communications involving mobile apps, digital communications channels, and digital asset and cash management accounts communications.

That communications section also covers MSRB Rule G-21 concerning advertising by brokers, dealers or municipal securities dealers.

FINRA outlined general standards regarding false, misleading or promissory statements or claims. For example, do a firm's communications include material information necessary to make them fair and balanced and not misleading?

Exam findings for municipal securities communications show firms “using false and misleading statements or claims about safety, unqualified or unwarranted claims regarding the expertise of the firm, and promissory statements about claims regarding portfolio growth,” according to the report.

To address these concerns, FINRA pointed to some effective compliance practices for municipal securities advertisements including prior approval, training, risk disclosure, and review.

Essentially, FINRA suggests that firms require “prior approval of all advertisements concerning municipal securities by an appropriately qualified principal to confirm the content complies with applicable content standards.”

In terms of risk disclosure, an effective practice identified by FINRA is “balancing statements concerning the benefits of municipal securities by prominently describing the risks associated with municipal securities, including credit risk market risk and interest rate risk.”

Additionally, FINRA’s report suggested that firms should provide education and training on applicable FINRA and MSRB rules and their firm’s policies regarding municipal securities advertising.

According to FINRA, this means that firms should also review their communications to “confirm that the potential benefits of tax features [of municipal securities] are accurate and not exaggerated.”

By Kelley R. Taylor

BY SOURCEMEDIA | MUNICIPAL | 02/09/22 01:53 PM EST

MSRB's ESG Request for Information Begins to Collect Submissions.

Responses to the Municipal Securities Rulemaking Board’s request for information on environmental social and governance factors are beginning to show some indication of the challenges regulators face in responding to the growing interest in ESG investing.

Responses to the MSRB’s December RFC so far have generally agreed that standardized ESG disclosures would add quite the workload for issuers, as was identified in the Government Finance Officers Associations best practices.

“When you mention ESG there’s probably four different directions you can go with that and that’s a challenge I think the market has,” said Dave Erdman, capital finance director for the State of Wisconsin.

Many of these concerns were mentioned during GFOA’s winter meeting, as many have remarked how broad ESG disclosures can be and how burdensome they may become should the MSRB or others decide they are necessary.

“It is not that issuers do not want to report ESG factors, but for many there are so many approaches which creates disorientation and questions about what is material or important,” said Dan Aschenbach, principal consulting partner at AGVP Advisory in his submission.

Some issuers are already beginning to submit responses on what kind of disclosures make sense for them.

“Voluntary disclosures make the most sense for the municipal market,” the City of Detroit said in its response, the only issuer to submit so far. “We agree with the GFOA guidance that standardized ESG disclosures would be overly burdensome, costly, and potentially inhibiting for municipal issuers who could decide not to use ESG designations they deserve to avoid the added cost and effort.”

But the matter of disclosure becomes slightly more complicated as it relates to the issuance of social bonds.

The City of Detroit issued $175 million in 2021 in social bond designation “based on the intended use of the bonds for the financing of blight removal purposes,” the submission said.

The City’s Social Bonds Designation follows the “Social Bond Principles,” as promulgated by the International Capital Market Association, updated most recently in June 2020.

“The proceeds of the bonds are funding projects consistent with a number of these categories, including affordable housing, employment generation and socioeconomic advancement and improvement, which is expected to benefit certain of the target population included by the ICMA in the Social Bond Principles,” the city said.

The City of Detroit decided to use ICMA standards saying they were “clear, easy to follow and fit our purpose.” The issuer also did not consider using a third-party vendor to certify the bonds as they “did not feel doing so would add any value or be a good use of money.”

Detroit also intends to disclose annually with EMMA on the spending of those bonds with the Social Bond designation, despite it not being required by the City. They also indicated the potential disparities that may arise from a dependence on ESG data vendors.

“Vendors that certify ESG Municipal Securities could cause a disparity in markets because small issuers may not be able to afford their services,” the submission said. “Such certification essentially price out issuers who would otherwise sell ESG bonds.”

The MSRB is also being asked to consider the matter of “greenwashing,” which the Securities and Exchange Commission is expected to address this year. Greenwashing refers to a misleading labeling of something as environmentally sound.

“Self-certification or examination in the private sector resulted in ‘greenwashing’ and now there are calls for disclosure regulation on what gets published,” AGVP?s Aschenbach said in his submission.

“The question remains in the private sector on what is material and relevant,” he added. “The municipal bond sector should recognize the potential for ‘municipal greenwashing’ and with limited municipal staff, understand the strain on ESG self-reporting.”

In the City of Detroit?s view, ESG considerations are very different in the corporate and public sectors and further guidance should reflect that.

“ESG considerations in the corporate sector are very different than in the public sector, and the type and frequency of disclosures should not be the same,” the City of Detroit submission said. “The vast majority of municipal bonds clearly serve an ESG purpose; whereas the vast majority of corporate bonds do not.”

“Corporate issuers who seek to use an ESG designation should be required to meet certain disclosure requirements, which are unnecessary for municipal issuers given the fundamental public purpose that municipal bonds serve by definition,” the City of Detroit said.

Other submissions seek to address how one might seek to address historic ills in the financial system with the use of ESG designated bonds.

“An investor seeking to identify bonds that explicitly created racial and social equity, how would she do so?” said Joyce Coffee, president and founder of Climate Resilience Consulting in her submission. “The S in ESG frequently identifies projects that improve health, education or workforce outcomes,” she added. “However, these outcomes could be ascribed to any demographic.”

The MSRB is collecting responses until March 8.

By Connor Hussey

BY SOURCEMEDIA | MUNICIPAL | 02/04/22 01:49 PM EST

MSRB Announces Members of 2022 Board Advisory Groups.

Read the press release.

SEC’s Gensler: Major Cybersecurity Regulatory Changes On the Horizon

Summary

A significant expansion of rules relating to cybersecurity risks—particularly for the financial sector—is under consideration by the Securities and Exchange Commission (SEC).

In public remarks last week, SEC Chair Gary Gensler previewed a number of areas in which the SEC is looking to “broaden and deepen” its oversight of cybersecurity practices and risks. They range from a broad expansion of system integrity rules to changes involving the timing and delivery of privacy notices. Although new rules governing cybersecurity disclosures have been anticipated for months, Gensler’s remarks indicate that the SEC’s plans go well beyond disclosure rules and are far more ambitious.

Significant Changes Likely for the Financial Sector and Its Service Providers

Extension of Reg SCI to “Large, Significant” Entities. One of the most far-reaching changes being considered involves broad expansion of the Regulation Systems Compliance and Integrity Rule (Reg SCI).

Reg SCI, adopted in November 2014, applies to entities that form the backbone of U.S. financial markets: self-regulatory organizations, including the securities and options exchanges, clearing agencies, FINRA, and the Municipal Securities Rulemaking Board (MSRB), as well as certain alternative trading systems (ATSs) and plan processors involved in distributing transaction and quotation information.

Reg SCI requires these covered entities to have policies and procedures in place to protect systems integral to key market functions: trading, clearance and settlement, order routing, market data, market regulation and surveillance. Reg SCI also requires covered entities to take corrective action and immediately notify the SEC if certain events occur. It also requires them to provide quarterly

reports, conduct annual reviews and tests, and maintain books and records.

According to Gensler, the SEC is considering expanding Reg SCI to include "large, significant entities" such as market-makers, broker-dealers and Treasury trading platforms. The SEC took the first step just days after Gensler's speech and proposed new rules that would require ATSs that trade government securities to comply with Reg SCI.

The other "large, significant entities" that might become subject to Reg SCI remain to be seen. Large market-makers and broker-dealers will certainly be on the list, but other large entities supporting these market functions should be watching developments closely. Even if these entities already have sophisticated controls in place, the additional event notification, reporting, review and testing required by Reg SCI—all under the SEC's scrutiny—will present additional challenges.

Gensler also announced that the SEC is looking at ways "to deepen" Reg SCI to "shore up the cyber hygiene of important financial entities." He provided no further details, so it is not clear what the SEC is planning to do here. Perhaps specific technical safeguards will be required, such as encryption and multi-factor authentication, along with other such measures.

New Rules for Investment Companies, Investment Advisers and Broker-Dealers. Beyond Reg SCI, Gensler also announced that the SEC is considering new rules for investment funds, advisers and broker-dealers. Here, the SEC is focusing on ways to strengthen "cybersecurity hygiene and incident reporting." These changes would ensure entities continue to operate during significant incidents, provide clients and investors with better information, give the SEC "more insight into intermediaries' cyber risks," and create incentives to "improve cyber hygiene." Gensler offered no particulars but indicated that guidance was being drawn from the Cybersecurity and Infrastructure Security Agency (CISA) and "others." The "incentives" proposed to improve "cyber hygiene" will be of particular interest. They could range anywhere from safe harbors that encourage reporting to new attestation requirements with strict penalties.

Expanded Authority Over Financial Sector Service Providers. Another potentially far-reaching change being considered would give the SEC authority over third-party service providers that provide various administrative and technical services to financial sector registrants. Here, the SEC is reportedly considering "a variety of measures" such as requiring registrants to identify service providers that might pose cyber risks, and holding registrants accountable for service providers' cybersecurity measures.

Gensler, however, also expressed interest in a far more sweeping change: giving "market regulators" the same type of power over third-party service providers that bank regulators have under the Bank Service Company Act. That Act subjects third parties performing certain services for banks, (e.g., data processing, Internet banking and mobile banking services), to regulation and examination by the bank regulators to the same extent as the banks themselves. If enacted, such a law potentially would give the SEC authority over the systems and operations of cloud service providers and payment processors, to name a few.

Reg S-P Notifications. According to Gensler, the SEC is also looking at ways to "modernize and expand" Reg S-P. Currently, Reg S-P requires brokers, dealers, investment companies and advisers to provide privacy notices to customers and have written policies and procedures in place to safeguard customer information. The potential changes, Gensler explained, would relate to how notification is given to clients when their personal information has been accessed, as well as the "timing and substance of notifications currently required." Although not entirely clear, the SEC may be considering a new breach notification rule as well as updates to existing privacy notice forms.

Gensler also confirmed that the SEC is looking at new rules involving cybersecurity risk disclosures and practices that would be applicable to all public companies.

Cybersecurity Risk Disclosures. According to Gensler, the SEC is considering ways in which cybersecurity risk information can be presented by issuers in a "consistent, comparable, and decision-useful manner." The SEC also is examining "whether and how to update disclosures" when cybersecurity events have occurred. Although no specifics were provided, proposed mandatory disclosures for cybersecurity risks, along with guidance for assessing the materiality of cyber events, may be expected.

Cybersecurity Practices. The SEC is also apparently preparing recommendations around company practices with respect to "cybersecurity governance, strategy, and risk management." These issues have been the subject of SEC guidance, risk alerts and enforcement actions for the past several years. Look for proposed rules addressing internal controls for reporting cybersecurity risks and incidents and additional safeguards to protect customer information.

The SEC has staked out a very ambitious cybersecurity agenda for the months ahead. We'll be following developments and provide updates as they occur.

Bryan Cave Leighton Paisner LLP – Lori Van Auken

January 31 2022

Municipal Securities Regulation and Enforcement: The Year in Review and a Look Ahead - Ballard Spahr

The municipal securities market carried its momentum from the first half of 2021 into a strong finish for the year against the backdrop of continued regulatory and enforcement actions. Despite new variants of COVID-19 emerging, which continue to impact travel, commerce, and the economy, the municipal market continued its strong upward trajectory, spurred by continued low interest rates and the anticipated injection of federal funds to state and local issuers as part of the Infrastructure Investment and Jobs Act.

View pdf.

GFOA Member Alert: Tier 1-3 SLFRF Project and Expenditure Report Due January 31

If your organization is a Tier 1-3, GFOA strongly recommends filing by the deadline. Completing the report as early as possible will ensure your jurisdiction will not be considered late, which may lead to a finding of non-compliance.

LEARN MORE

MSRB Votes to Extend Pandemic Relief and Implement a New Approach to Fees at Quarterly Board Meeting.

The Municipal Securities Rulemaking Board (MSRB) met virtually January 26-27, 2022 for its quarterly Board of Directors meeting, where the Board voted to extend certain temporary pandemic regulatory relief and refine its approach to the fees that enable the self-regulatory organization (SRO) to fulfill its mission to safeguard the $4 trillion municipal securities market. The Board discussed several other ongoing initiatives to advance the four goals outlined in its long-term strategic plan.

Regulatory Initiatives

"Our nation's schools, hospitals and workplaces continue adapt to challenges presented by the pandemic," said MSRB Chair Patrick Brett. "The MSRB has been operating fully remotely for nearly two years, and we appreciate the challenges posed to regulated dealer firms of conducting traditional in-person office inspections when their employees are working from remote offices."

The Board voted to propose amending MSRB Rule G-27 to allow dealer firms to conduct office inspections remotely until December 31, 2022. This additional six-month extension would align with a similar extension that the Financial Industry Regulatory Authority (FINRA) filed with the Securities and Exchange Commission (SEC) earlier this month. Previous MSRB actions to provide temporary regulatory relief, data and information to support market participants during the pandemic are available on the MSRB's dedicated COVID-19 information page on its website.

Also at its meeting, the Board determined to seek SEC approval of a proposal to implement structural changes to the organization's approach to managing fee revenue and reserve levels to ensure a fair, equitable and sustainable balance of funding that will support its mandate to protect investors, issuers and the public interest.

As detailed in the MSRB's FY 2022 Budget and FY 2021 Annual Report, the majority of the MSRB's revenue comes from market volume-based fees on regulated entities, which has contributed to a cycle in which the MSRB accumulates excess reserves and then implements temporary solutions such as fee rebates and temporary fee reductions.

"We share regulated entities' frustration with this cycle, which we addressed most recently with the largest temporary fee reduction in MSRB history that is on target to return $19 million in accumulated excess reserves to the industry by the end of this fiscal year," Brett said. "Under the leadership of the Finance Committee and with the benefit of input from regulated stakeholders, the Board has undertaken a comprehensive examination of our finances."

Finance Committee Chair Frank Fairman said, "We have developed an approach that maintains a sustainable financial model, adequately funds future expenses and, most importantly, mitigates the impact of market variability, providing a better mechanism for effectively managing reserve levels." The MSRB plans to seek SEC approval of the new approach with an eye toward implementing it at the beginning of FY 2023.

The Board also met with FINRA President and CEO Robert Cook to discuss continued regulatory coordination on matters related to the municipal securities market.

Transparency Initiatives

The Board previewed preliminary concepts for a new user interface for the free Electronic Municipal Market Access (EMMA®) website based on extensive input from stakeholders.

“We are in the early stages of a complete transformation of the EMMA website that aims to make the market’s official online source for data and disclosures easier to navigate and more intuitive to use,” Brett said. “In the meantime, EMMA users can expect to see continued incremental improvements based on their feedback about pain points, such as recent improvements to help issuers more easily manage the process of associating individual securities to a disclosure filing in EMMA.” To help keep stakeholders informed of upcoming and longer-term EMMA enhancements, the MSRB now publishes a forward roadmap of its transparency and technology initiatives on its website.

Market Structure and Data

The Board also discussed a number of market structure topics, including price transparency considerations raised in the SEC’s recent proposal to amend Regulation ATS and the MSRB’s ongoing work to evaluate market feedback and data to understand the prevalence of pennying in the municipal market. This practice involves a dealer’s purchase of bonds for its own account from a customer seeking to sell a municipal security—after the dealer has reviewed other dealers’ bids—by matching a high bid or purchasing the bond at a price that is nominally higher than the highest bid.

The Board also discussed early feedback on EMMA Labs, the MSRB’s new innovation sandbox, where market stakeholders can collaborate with MSRB staff to test active prototypes, help improve their utility and accelerate the pathway to bring enhanced market transparency tools to life on the EMMA website.

Public Trust

The Board discussed engaging with stakeholders on emerging market topics and also discussed the work of its standing committees, including the Nominating Committee’s efforts to solicit applications through February 7, 2022, for two public members and two regulated members of the Board.

“One of the most important jobs for an SRO is selecting a new class of market experts to join us in overseeing the long-term strategic direction of the organization,” said Meredith Hathorn, MSRB Vice Chair, and Chair of the Board’s Nominating Committee. “The four new members who will join our Board for FY 2023 will have the opportunity to help advance our thinking on a number of critical topics for our market. We’re making great strides in leveraging technology and structured data to support informed decision-making, and we’re in the early stages of gathering information on Environmental, Social and Governance (ESG) practices and developing strategies to advance Diversity, Equity and Inclusion (DEI) in the municipal securities market.”

Date: January 28, 2022

Contact: Leah Szarek, Chief External Relations Officer
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MSRB Launches Emma Labs as the Regtech Innovation Sandbox for the Future Of Municipal Bond Market Transparency.

Washington, DC – The Municipal Securities Rulemaking Board (MSRB) today launched EMMA Labs, its innovation sandbox for transparency enhancements for the $4 trillion municipal securities market. EMMA Labs enables investors and other market data users to test and develop prototypes

collaboratively and provide feedback. The goal is to enhance the utility and accelerate the deployment of potential data analytics tools on the MSRB's Electronic Municipal Market Access (EMMA®) website , which provides free public access to real-time trade data and disclosures from tens of thousands of state and local governments and other entities.

"We are excited about EMMA Labs' potential to drive collaboration with market participants and allow us to co-create the future of municipal market transparency," said MSRB Chair Patrick Brett. " EMMA Labs is a key part of the MSRB's strategic plan to leverage data to deepen market insights and facilitate regulatory modernization – and it opens up a technological pathway for engaging with stakeholders on opportunities for strengthening our market to serve the public interest."

EMMA Labs serves as a proving ground for functional prototypes, called Active Labs, that could ultimately be deployed on the EMMA website. EMMA Labs is debuting with two Active Labs:

- A keyword search engine that unlocks the information contained within hundreds of thousands of disclosures submitted to the EMMA website as unstructured PDFs, and
- A dynamic dashboard for market data analysis that empowers users to discover and visualize market trends.

"With EMMA data now in the cloud, we will increasingly be able to leverage technology to create powerful analytical tools that empower data users to better identify, visualize and understand market trends," said Brian Anthony, MSRB Chief Data Officer. "The first Active Labs are an invitation to collaborate: Any individual can create a free EMMA Labs account to provide feedback on prototypes, and we welcome ideas for future Active labs, tools and partnerships."

The MSRB will host recurring virtual Innovation Office Hours to discuss ideas submitted through EMMA Labs.

Date: January 19, 2022

Contact: Leah Szarek, Chief External Relations Officer
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Draft Companion Compliance Resources for Dealers and Municipal Advisors.

SUMMARY

SIFMA provided comments to the Municipal Securities Rulemaking Board (MSRB) Notice 2021-12 requesting comment on draft companion compliance resources for brokers, dealers and municipal securities dealers and municipal advisors.

View the SIFMA comment letter.

SEC Taking a Closer Look at Issuer Disclosure.

The Securities and Exchange Commission's acting director for its Office of Municipal Securities singled out disclosures related to its Rule 15c2-12 as an area the office is watching closely, following

an academic study that found serious deficiencies in continuing disclosure.

Ernesto Lanza raised that subject in his remarks before the Government Finance Officers Association's Committee on Governmental Debt Management during GFOA's 2022 Winter Meeting.

"We think it needs to be more refined," Lanza said. "We think there's more to be looked into in that area. If there are ambiguities in the rules, we should have conversations around that. If there are people who need redouble efforts then we think they need redouble efforts," he added. "So that's an important thing."

The concern is over two 2019 amendments to SEC Rule 15c2-12, which require bond issuers to disclose the incurrence of a financial obligation of the issuer or obligated person, if material, in addition to any agreements to covenants, events of defaults, remedies, priority rights or other similar terms of a financial obligation of the issuer or obligated person, if material.

This matter caused some stir at the Brookings Municipal Finance Conference last year, when Federal Reserve economists Ivan Ivanov and Nathan Heinrich, in addition to the University of Cologne's Tom Zimmermann asserted that there was pretty significant underreporting under the two new provisions and that it remains a significant risk for investors.

Lanza acknowledged the Commission's efforts to quell the concerns that came out of the conference and further guidance on the issue may very well be on the way.

"We continue to think that disclosure is an important area to help provide some guidance," Lanza said.

A GFOA Committee Member remarked that during their time in the muni market, general disclosures have improved over time, but things are still not perfect. "We're always looking for ways we want to make it better," Lanza said. "And I think improvements are not across the board."

"I'd like to have some input and discussions around where the rough edges are," Lanza said. "Again, it looks relatively simple on paper but it is fairly complex to analyze what's in what's out and what needs to be disclosed." Lanza said.

The topic of disclosure eventually led participants to press Lanza on the Commission's as well as the Municipal Securities Rulemaking Board's efforts concerning ESG, a matter recently highlighted in the Board's request for information on ESG, which some believe is overstepping its boundaries and convoluting the matter even further.

"I think it's important for them to get whatever they think is important information and research and market input in order to make decisions on whether or not they undertake rulemaking or not," Lanza said.

"I don't adhere to the view that they can only ask questions on things that are directly related to a specific proposal that they're undertaking," he added. "I think they need to understand the marketplace to be able to undertake rulemaking."

But there is a line. "That doesn't speak to what they do with the information afterwards," Lanza said.

Ultimately the Commission leaves the MSRB to conduct its own fact finding mission if it hopes to provide further rulemaking on a particular issue. As for the SEC, there are no immediate plans to enact further rules, though they are keeping their eyes peeled.

“There’s nothing on the agenda for us right at this moment, although we’re obviously paying attention to that,” Lanza said. “It can change from day to day in terms of what we’re asked to do.”

“It bothers me sometimes when sometimes, participants get the impression that there are certain comments that regulators don’t want to hear,” Lanza added. “We need to hear everything.”

Lanza also said he champions efforts to provide more transparency in fixed income markets.

“There are existing transparency systems for post trade transactions,” Lanza said. “We want to explore with the two SROs, FINRA and the MSRB, potential incremental improvements on the data flow, data quality, timeliness and the extent of the information.”

“Clearly, those are areas that are not of direct concern to the municipal securities issuer community, but certainly have significant knock on effect in terms of efficiency of pricing, and that ultimately will have, if nothing else, potential impact on pricing and new issues down the line,” he added. “We think that’s an important thing to keep in mind.”

By Connor Hussey

BY SOURCEMEDIA | MUNICIPAL | 01/24/22 01:12 PM EST

Treasury's Letter to Arizona May Impact Muni Issuance Disclosures.

The Department of the Treasury’s Friday letter detailing its intentions to clawback some of Arizona’s COVID-19 relief aid if the state doesn’t redesign two of its pandemic-related programs may impact the disclosure of any state facing the prospect of a fight over those funds.

The American Rescue Plan Act’s final rule on how its State and Local Fiscal Recovery Fund Program may be used included a provision which would deem programs, including using the stimulus funds to offset tax cuts, as “ineligible uses”. The letter to Arizona Gov. Doug Ducey indicated that two programs, one being the $163 million grant program for schools that follow state laws banning public school mask mandates, would fall in that category.

“This is a unique situation since the letter was addressed to the state,” said Eryn Hurley, deputy director of government affairs at the National Association of Counties. “Under ARPA, the state was allocated a portion of the funds and the counties were given their own allocations.”

The American Rescue Plan Act allocated $65.1 billion to counties, which is separate from the state allocation and dispersed directly from the Treasury to the counties. Since the letter is addressing actions at the state level, its impact will largely stay at the state level and won’t bleed into counties, Hurley said.

According to Dave Erdman, capital finance director for the State of Wisconsin, the Treasury’s move to reign in Arizona shows they’re willing to enforce the exact language on ARPA and SLFRF.

“From a municipal bond issuance perspective, it’s clear that the Treasury will threaten and use these programs that came out of the ARPA,” Erdman said. “But the biggest question is in regards to disclosure.”

“How does a clawback of such need to be disclosed?” he added. “If the State of Arizona was going to

do a public offering, or any state threatened with clawback, how do you get this information to investors, because it could be material."

A clawback at the state level could then affect future bond offerings, Erdman said, if a state was preparing an offering then gets hit with a clawback from Treasury.

"Treasury has to be careful when making those kinds of statements because it could scare investors and have an impact on the pricing of a transaction," Erdman said.

The Treasury letter gives the State of Arizona 60 days to remedy its two related programs, which from Ducey's Twitter response, doesn't seem likely.

"When it comes to education, President Biden wants to continue focusing on masks," he wrote. "In Arizona, we're going to focus on math and getting kids caught up after a year of learning loss."

"We will respond to this letter and we will continue to focus on things that matter to Arizonans," he added.

By Connor Hussey

BY SOURCEMEDIA | MUNICIPAL | 01/18/22 02:47 PM EST

Hawkins Advisory: Final Treasury Reissuance Regulations Addressing Modifications of Debt Instruments to Replace IBORs

Attached is a Hawkins Advisory describing recently released final Treasury Regulations providing guidance in connection with the reissuance consequences arising from modifications of existing debt instruments and other contracts to replace discontinued Interbank Offered Rates with alternative reference rates.

View the Hawkins Advisory.

An ESG Reckoning Could Be on the Horizon for Municipal Bonds.

The Municipal Securities Rulemaking Board, the self-regulatory organization over municipal bond issuers, has started a key first step on the way to regulation within the space. The MSRB has issued a Request for Information as of December, seeking to find out what ESG borrowers are disclosing regarding how their bonds relate to ESG, reports Bloomberg.

Municipal bonds related to ESG experienced a record year last year, bringing in $24.6 billion of green debt, the biggest portion of the ESG muni pie. However, an analysis done last year by a UN group found that borrowers weren't disclosing ESG data effectively or with any type of consistency, including risks that pertained to the environment and climate change.

Current ESG standards within municipal bonds are such that data and what is reported, as well as the frequency it is reported at, are all optional. The call for commentary, which is an appeal to public officials, bankers, investors, as well as the general public, focuses heavily on phrasing centered around the word "standard" or an iteration of it.

It's a bit of a writing on the wall situation and mirrors a larger call that the SEC put out in March 2021 requesting ESG commentary on climate disclosures by issuers. While no regulations have been forthcoming yet, analysts anticipate some sort of guidance at minimum to be released by the Commission this year.

The main culprit in drawing the regulatory attention within munis could be the very thing that brought in so much money to the space: green bonds. At their inception in 2013 when Massachusetts sold the very first self-styled green bonds to pay for a host of upgrades centered around energy efficiency, water quality, and pollution control, any state or local government could create a bond and decide that it was green without any oversight or standards. That's still mostly the case, though there have been some attempts at creating standards within the industry since.

"Many investors and other market participants are seeking ESG-related information beyond what historically has been provided to the market. In response, private vendors are offering ESG certification service," writes the MSRB in their statement.

The cropping up of private vendors centered around green bonds creates the potential for an uneven playing field for investors, with some investors having access to potentially better information, or even more information, than what is currently legally required. It's something the MSRB could be seeking to remedy in their Request for Information, and it remains to be seen what will come of the information gathered once the window closes for submissions.

ETF TRENDS

by KARRIE GORDON

JANUARY 5, 2022

GASB Adds Major Project, Pre-Agenda Research Area to Technical Plan.

Norwalk, CT, January 6, 2022 — During its December 2021 meeting, the Governmental Accounting Standards Board (GASB) approved the addition of a major project on going concern uncertainties and severe financial stress and pre-agenda research activity on subsequent events as part of its technical plan for the first third of 2022.

Going Concern Uncertainties and Severe Financial Stress

The GASB added this project based on the results of more than five years of research on the GASB's existing standards for going concern uncertainties and current practice with respect to identifying governments experiencing or in danger of severe financial stress.

The concept of going concern uncertainties was not specifically developed or significantly modified for the government environment when incorporated into the current GASB literature. Pre-agenda research indicates that, even when governments are in or have been experiencing severe financial stress, few dissolve or cease operations. Although current guidance provides that financial statement preparers have a responsibility to evaluate a government's ability to continue as a going concern, such an evaluation often poses challenges and has resulted in diversity in practice. These challenges also include determining whether or when governments have a responsibility to evaluate and disclose their exposure to severe financial stress.

The objectives of the project are to consider (1) improvements to existing guidance for going concern considerations (including the definition of a going concern) to address diversity in practice and clarify the circumstances under which disclosure is appropriate, (2) developing a definition of severe financial stress and criteria for identifying when governments should disclose their exposure, and (3) what information about a government's exposure to severe financial stress is necessary to disclose.

Subsequent Events

The objective of the pre-agenda research item on Subsequent Events is to (1) evaluate the effectiveness of the existing guidance for identifying and reporting subsequent events and (2) consider the need for revisions to those standards. If additional guidance is determined to be needed, another objective would be to consider the development of revised accounting and financial reporting for subsequent events.

As part of its consideration of the first-third 2022 technical plan, the GASB also considered but chose not to add (1) a project on interim financial reporting and (2) a pre-agenda research activity on related-party transactions.

More information on the new project and pre-agenda research activity is available on the GASB website under the Technical Plan section.

Muni Market's Regulator Is Seeking Standards for Disclosure on ESG Debt.

- **MSRB asks for feedback on how issuers disclose credit risk**
- **Government finance officers released best practices in 2021**

There's a big mess in MuniLand, and the Municipal Securities Rulemaking Board wants to clean it up.

The mess is "Environmental, Social and Governance" practices by municipal issuers, and the MSRB, the self-regulatory organization in charge of the $4 trillion market, wants feedback — from bankers to public officials to investors and the general public — about what borrowers disclose on how ESG relates to their bonds.

The MSRB put out its Request for Information in December, and said it wants comments by March 8. It's an issue that Mark Kim, the MSRB's chief executive officer, flagged back in September as ESG munis were headed for a banner year: Issuance of green debt alone, the largest part of the muni ESG segment, totaled a record $24.6 billion in 2021, data compiled by Bloomberg show. But one analysis last year found that borrowers don't disclose relevant data consistently or effectively, such as risks related to the environment.

The regulator's request for comment contains the word "standard" or a variation at least nine times. It also uses terms such as uniform and metrics. So you can see where this may be going — ultimately, the establishment of disclosure standards.

Right now, as is typical in the municipal market, everything is optional. The MSRB reminds readers that it is charged with enhancing both issuer and investor protection and "the overall fairness and efficiency of the municipal securities market." So the current state of affairs will never do, at least according to the MSRB.

Self-Styled Issuance

I blame green bonds for the regulatory interest in this topic. The securities are increasingly common in the U.S. corporate market, where investors are pushing for more sustainable debt. Municipal borrowers began offering them in 2013, when Massachusetts sold $100 million in self-styled green bonds to pay for improvements to water quality, energy efficiency and pollution control, according to the MSRB website.

Now, I always saw most munis as green bonds, used to improve the environment in some fashion. The key term in that description in the paragraph above was "self-styled." States and local governments seemed eager enough to slap the green label on certain bond issues, and when you'd ask them about it, about who decided what was a green bond, it turned out that they did. It was a marketing tool, and if certain investors were willing to go out of their way to buy a municipal bond labeled "green," well, terrific! There was no standard to it, no independent verification. At least, not at the beginning, and even now, not uniformly.

As the MSRB's request makes clear, that may be about to change.

"Many investors and other market participants are seeking ESG-related information beyond what historically has been provided to the market. In response, private vendors are offering ESG certification services." And you can stop right there. Once there's a multiplicity of sources for information, there's the possibility that some investors will get more or better information than the legally required disclosures in offering documents. The MSRB request lists five private vendors who currently certify green bonds, including Build America Mutual, Kestrel Verifiers and Sustainalytics.

And then toward the end of the request, the MSRB asks bluntly whether the ESG indicator from IHS Markit that it has incorporated on its EMMA website's new-issue calendar enhances market transparency. And then it asks, "What improvements could the MSRB make to the EMMA website regarding ESG-Related Disclosures, ESG-Labeled Bonds and other ESG-related information?"

Best Practices

The Government Finance Officers Association in 2021 released best practices concerning ESG disclosure, and best practices aren't just concocted overnight, so I asked them about it. Keep in mind that the MSRB in a footnote in its request quotes the GFOA as citing the impracticality of developing uniform metrics to gauge risks.

"One thing that stood out to us is the RFI at times tends to blur the bright line that exists between two things: 1. ESG disclosures on everyday bonds issued and 2. Designated Bonds (i.e. green or social bonds) which are designed to be issued for specific purposes," wrote Emily Swenson Brock, director of the GFOA's Federal Liaison Center, in an email. "We will do our best to clarify that bright line (by pointing to our best practices here) and provide the MSRB ideas on how the municipal bond industry can work together to advance issuer awareness and practice in ESG."

And Dave Erdman, Wisconsin's capital finance director and a member of the GFOA Debt Committee, said in an email, "Yes some metrics or standardization of criteria and requirements that must be met to have designated bond (such as green, social, etc) would be beneficial to all, in other words, everyone is playing the same game and aiming for the same fences when designating a bond, but do we really want to open the regulatory and reality door on standardization of disclosure language?"

It's clear that the age-old fight between the analysts who want more and issuers who already feel beleaguered by their demands is about to enter a new phase.

Bloomberg Markets

By Joseph Mysak Jr

January 5, 2022, 9:45 AM PST

— With assistance by Danielle Moran

(Joe Mysak is a municipal market columnist who writes for Bloomberg. His opinions do not necessarily reflect those of Bloomberg LP and its owner, and his observations are not intended as investment advice.)

NFMA's Diversity, Equity & Inclusion Initiatives.

The DEI Committee began work in 2021 on initiatives to promote Diversity, Equity & Inclusion in the NFMA. The first priority was to propose a new mission statement to be incorporated into the NFMA constitution. Effective December 27, 2021, the NFMA's constitution was amended with the new mission statement. To read the current NFMA constitution, click here.

For a better understanding of the goals of the DEI Committee, watch this short report by Anne Ross, 2021 NFMA Chair, Neene Jenkins and Nicole Byrd, Co-Chairs of the DEI Committee. For more information about the NFMA's DEI initiatives click here.

IRS and Treasury Guidance On the Transition From Interbank Offered Rates to Other Reference Rates.

Read the guidance from the IRS and Treasury.

IRS and Treasury Release Final Guidance on Libor Transition.

The Internal Revenue Service and Department of the Treasury have released final guidance on the transition away from Libor, setting Secured Overnight Financing Rate as an alternative and creating noncovered modification in the place of fair-value.

The cessation of Libor matters to the muni market because existing debt and contracts may reference it, potentially impacting variable-rate debt, swaps and contracts, among other things.

The final regulations hope to swap out the Libor rate that is no longer being published as of Dec. 31, 2021, but will be around until June 2023, with a new formula that won't change the economics of the deal or cause reissuance of the particular debt.

"It seems to follow pretty closely the recommendations of the Alternative Reference Rates Committee, the New York Fed group that's overseeing the Libor transition and it seems to provide needed flexibility for municipal issuers who may need to change the terms of outstanding deals in order to accommodate the loss of Libor without having to undergo a reissue," said Michael Decker,

senior vice president of federal policy and research at the Bond Dealers of America.

“I think that’s the main thing that the community was looking for and I think it’s something that generally the community will be supportive of.”

The proposed regulations, released on Oct. 9, 2019, leaned on fair market value to ensure the value of the debt stayed the same.

“How do you differentiate changes that are just swapping out the old formula for the new formula?,” said Johnny Hutchinson, partner at Squire Patton Boggs and member of the National Association of Bond Lawyers’ board of directors. “The way that the Proposed Regulations tried to do that was to say, the fair market value of your debt has to be the same, both before and after the change.”

“But people get very skittish when you hand them a certificate signed that says these bonds are being sold at fair market value,” he said.

Muni market participants often say that calculating marked-to-market fair-value poses challenges for municipal bonds because they don’t often trade every day as stocks do. SOFR was another safe harbor outlined in the Proposed Regulations but has been somewhat controversial due to the short history of the formula being published, Hutchinson said.

With the final regulations, set to be published in the Federal Register on Jan. 4, the SOFR rate is mentioned as a qualified rate.

“A qualified rate is a SOFR-based rate or other qualified replacement rate, so long as it is in the same currency as the discounted IBOR or is otherwise reasonably expected to measure contemporaneous variations in the cost of newly borrowed funds in that currency,” law firm Cadwalader Wickersham & Taft said.

But satisfying the requirements with a constant fair market value has been changed.

“That requirement has been completely scrapped, it looks like from an initial read,” Hutchinson said. “Instead, the way that the Final Regulations are going to test whether the parties are really making changes beyond just swapping in a new formula for the old formula, is there are a list of what are called noncovered modifications and they all relate to changes in the timing or amounts of the cash flows on the debt.”

The shift in approach basically says as long as you don’t make these specific noncovered modifications, the IRS or Treasury won’t inquire as to whether the fair market value is the same.

But some modifications to existing agreements may include both covered and noncovered components, which should be tested on a standalone basis, the regulation says. In a way, this makes things a bit more definitive for bond counsel as when a modification event occurs, they’re able to pull up the list of noncovered modifications and see whether the specific event falls under it.

But still some uncertainty exists as bond counsel familiarize themselves with the long list of noncovered modifications. “If that’s how the regulations work, I think that’s a good thing,” Hutchinson said. “It’s helpful and it allows us to apply the rules with, a little bit more certainty than we had before.”

For issuers, this may result in additional time and money spent with bond counsel. “That’s what the attorneys do, they have to test whether or not they can be qualified,” Emily Swenson Brock, director of the federal liaison program at Government Finance Officers Association. “It’s hard because that

adds a lot of cost and it adds a lot of time."

There is currently legislation passing through Congress that could affect that would allow for non-penalized modifications to outstanding contracts when LIBOR ceases to exist in June 2023. It passed the House in December in a 415-9.

It follows New York State legislation that hopes to minimize disruptions by allowing "tough legacy" contracts or those that expire after June 2023 and do not have fallback language specifying an alternative to use SOFR.

In a letter to Speaker of the House Nancy Pelosi and Republican Leader Kevin McCarthy GFOA and many other industry groups hoped to tip the scale in the industry's favor. "Without federal legislation to address these contracts, investors, consumers, and issuers of securities may face years of uncertainty, litigation, and a change in value," the letter said. "This would thereby create ambiguity that would lead to a reduction in liquidity and an increase in volatility."

By Connor Hussey

BY SOURCEMEDIA | MUNICIPAL | 02:58 PM EST

NFMA's New Mission Statement Approved.

Effective December 27, 2021, the NFMA's constitution was amended to incorporate a new mission statement. To read the current NFMA constitution, click here.

NFMA Municipal Analysts Bulletin - December 2021

Volume 31, No. 3 of the NFMA newsletter is available by clicking here. Also, please click here to read the special edition of the NFMA Municipal Analysts Bulletin, dated October 26, 2021. This special edition was published to provide NFMA members notification that the NFMA Board of Governors have approved a change to the NFMA mission statement, which represents an amendment to the NFMA Constitution. The proposed amendment is subject to a 60-day comment period by NFMA Regular Members.

RBC Paying $1M FINRA Settlement for Years of Junk Bond Oversight.

A brokerage firm accused of failing to track "junk bond" overconcentration in customer accounts for years has agreed to pay $1 million to settle with FINRA.

The regulator has sanctioned RBC Capital Markets, a New York-based broker-dealer with 2,400 registered representatives in its 275 branch offices, in a case involving potentially unsuitable concentration levels of high-yield bonds in customer accounts between July 2013 and June 2016.

During that period, RBC did not implement a supervisory system to comply with FINRA and Municipal Securities Rulemaking Board rules related to recommendations of high-yield corporate

and municipal bonds, according to a letter of acceptance, waiver and consent from FINRA.

As a result, the firm failed to flag more than 100 customer accounts with conservative profiles for this kind of activity.

Additionally, FINRA officials said they have repeatedly reminded member firms of their sales practice obligations in connection with high-yield or "junk" bonds because of the increased risks. These bonds receive lower credit ratings, indicating a higher risk of default.

In settling the case without admitting or denying the charges, RBC agreed to a censure, $456,155 plus interest in restitution and a $550,000 fine. The case originated from a FINRA cycle examination of RBC.

According to the FINRA letter, RBC changed the tax coding of municipal bonds in its system in July 2013. This coding change inadvertently disabled alerts to identify potential concentration issues for further assessment.

RBC did not detect that the alerts were not working, in part, because the firm did not test its alerts during the relevant period, the FINRA letter alleges.

The defective alerts were discovered in September 2015, but the firm allegedly did not address the issue until July 2016. RBC is accused of failing to adopt alternate measures to identify potentially unsuitable concentrations in high-yield bonds and failing to tell supervisors that the alerts were not working as intended.

John Gebauer, president of the compliance firm National Regulatory Services, said this case highlights the importance of thoroughly testing written supervisory policies and procedures as part of the annual 3120 review.

"It appears that RBC thoughtfully designed a supervisory control system and implemented automated controls to ensure that the policies were followed," Gebauer said. "However, when firms implement a technology-based solution, that does not eliminate the need to regularly test the systems to be certain that they are operating as intended. Whether by bug or changing requirements.

"This unquestioning deference to the results of technology is, unfortunately, an increasingly common occurrence."

In a number of the impacted accounts, the holdings in high-yield bonds were more than six times the thresholds set by the firm, according to the FINRA letter.

"For example, Customer M, who was over 100 years old, was a trustee for two trust accounts, both of which had the most conservative investment objectives. By June 2015, 86% of one trust account and 100% of the second trust account consisted of high-yield municipal bonds," said the FINRA letter.

The regulator then described another customer who was more than 70 years old and had a joint account with a conservative investment objective that, at times, consisted of as much as 92% in high-yield bonds.

Financial Planning has reached out to RBC Capital Markets for comment.

Financial Planning

By Justin L. Mack

December 21, 2021

FINRA Fines RBC Over $280,000 for Violating Muni Rule.

RBC Capital Markets, LLC agreed to pay more than $280,500 to settle Financial Industry Regulatory Authority charges that it violated the Municipal Securities Rulemaking Board's suitability rules when it failed to establish, maintain, and enforce a supervisory system with respect to high-yield municipal bonds.

In a December 14 Letter of Acceptance, Waiver and Consent (AWC), RBC agreed to pay a total fine of $550,000, plus restitution and interest of over $450,000 and to be subject to a censure.

In so doing, RBC neither admitted nor denied FINRA's findings that it violated NASD Rule 3010(a) and 3010(b) and FINRA Rules 3110(a) and (b) and 2010 with respect to the firm's supervision of high-yield corporate bonds, and MSRB Rules G-27(b) and (c) with respect to high-yield municipal bonds.

Specifically, FINRA found that for a period of three years, from July 2013 to June 2016, RBC, which has been a FINRA regulated broker-dealer since 1993, failed to identify for review, more than 100 customer accounts that had conservative profiles for potentially unsuitable concentration levels of high-yield bonds, i.e., those with a higher risk of default.

Under MSRB Rule G-27(b), municipal dealers are required to establish and maintain a supervisory system, which includes written supervisory procedures that reasonably ensure compliance with applicable securities laws.

FINRA Rules 2111 and 3110(a) have similar requirements for supervision, diligence and suitability. For example, under FINRA Rule 2111, member firms must have a "reasonable basis to believe that a recommended securities transaction or investment strategies is suitable for a customer based on information obtained through reasonable diligence of the firm."

In this case, FINRA found that RBC's supervisory system did not flag recommendations that resulted in potentially unsuitable concentrations of high-yield bonds in certain customer accounts. FINRA also concluded the firm's procedures did not sufficiently address suitability factors that its representatives should consider before recommending high-yield bonds.

For example, FINRA said that for a number of years, RBC's procedures did not provide guidance as to what proportion of a customer's portfolio should be invested in those high-risk products.

Additionally, FINRA found that RBC had daily and monthly recommended automated alerts designed to identify potentially unsuitable concentrations of high-yield bonds. However, FINRA concluded the alerts did not function as intended because RBC changed the tax coding of municipal bonds in its system in 2013.

The change "inadvertently disabled the ability of the high-yield bond alerts to identify concentration issues for further assessment," FINRA said.

Additionally, FINRA concluded that RBC did not test its alerts and so was not aware the system

wasn't functioning properly. According to the AWC, the firm realized the problem in 2015, but did not fix the system until 2016 and failed to adopt alternate measures to identify potentially unsuitable concentrations in customer accounts in the meantime.

As a result, FINRA found that RBC "did not review more than 100 conservative customer accounts for potentially unsuitable concentrations of high-yield corporate and municipal bonds." Some of those accounts contained high-yield bond concentrations more than six times higher than the thresholds set by the firm.

Consequently, FINRA charged RBC with failing to establish, maintain and enforce a supervisory system reasonably designed to achieve compliance with the relevant MSRB rules and imposed a censure, fine, and restitution and interest as sanctions.

Regarding the AWC, Nicole Garrison, director of corporate content, communications and social media for RBC Wealth Management-U.S., said, "we are deeply committed to careful management of the wealth clients entrust to us. As a firm, we pride ourselves on having strong policies and procedures in place to protect our clients. In the rare instance those policies and procedures fall short, we take steps to address them."

Garrison added, "We fully cooperated with FINRA and are pleased to have amicably resolved this case. This matter involves restitution to just 20 accounts and an issue that occurred and was fixed more than five years ago."

By Kelley R. Taylor

BY SOURCEMEDIA | MUNICIPAL | 12/16/21 01:59 PM EST

MSRB EMMA Update to CUSIP Groups Feature.

Issuers – we heard you. In response to stakeholder feedback the MSRB has introduced a completely redesigned "CUSIP Groups" feature that allows issuers to save a group of CUSIPs to use for future disclosure filings submitted to the EMMA.

Watch our tutorial.

MSRB RFC: New Draft Rule G-46

The MSRB is requesting a second round of comments on a new draft Rule G-46 to codify obligations of solicitor municipal advisors. Comments are due March 22, 2022.

Read the request for comment.

MSRB Opens Second Comment Period on Regulation of Solicitor Municipal Advisors: Cadwalader

The MSRB requested a second round of comments on revisions to proposed Rule G-46 ("Duties of Solicitor Municipal Advisors"). If adopted, the amendments would codify previously issued interpretive guidance concerning the requirements applicable to solicitor municipal advisors under Rule G-17 ("Conduct of Municipal Securities and Municipal Advisory Activities") (*see* related coverage).

In response to comments received during the first comment period, the MSRB is revising proposed MSRB Rule G-46 to (i) clarify that solicitor municipal advisors do not owe a fiduciary duty under the Exchange Act to clients in connection with solicitation activities and (ii) conform the rule to certain requirements that apply to non-solicitor municipal advisors and certain solicitations under IAA Rule 206(4)-1 ("Investment Adviser Marketing").

This new comment period will close on March 15, 2022.

December 16 2021

Cadwalader Wickersham & Taft LLP

Joint Trades Letter in Support of H.R. 4616, the Adjustable Interest Rate (LIBOR) Act.

SUMMARY

SIFMA in a joint letter with other associations, provided comments to the House of Representatives on the passage of H.R. 4616, the "Adjustable Interest Rate (LIBOR) Act," to address "tough legacy" contracts that currently reference LIBOR.

SIFMA signed with the following:

Structured Finance Association (SFA)
Bank Policy Institute
National Association of Corporate Treasurers
Education Finance Council
The Loan Syndications and Trading Association (LSTA)
The International Swaps and Derivatives Association (ISDA)
The Real Estate Roundtable
The Financial Services Forum
Institute of International Bankers
Government Finance Officers Association
Mortgage Bankers Association
Commercial Real Estate Finance Council (CREFC)
Consumer Bankers Association
Investment Company Institute
Institute for Portfolio Alternatives
Independent Community Bankers of America
U.S. Chamber of Commerce, Center for Capital Markets Competitiveness
Housing Policy Council
Student Loan Servicing Alliance
American Bankers Association

The American Council of Life Insurers (ACLI)

SEC Outlines Key Considerations for LIBOR-Linked Muni Securities.

A Securities and Exchange Commission staff statement issued Tuesday reiterates disclosure and fiduciary obligations of issuers and underwriters in light of the forthcoming transition away from Libor. And while those obligations are important, some municipal industry practitioners point to an already existing trend away from Libor-linked transactions.

Earlier this year, Libor's regulator, the Financial Conduct Authority, announced that it will cease the publication of 1-week and 2-month U.S. dollar Libor after Dec. 31, 2021. Remaining U.S. dollar Libors will cease in 2023.

The SEC staff statement "seems to be a restatement of existing obligations and requirements that apply to broker dealers and underwriters, both with respect to their issuer clients and their investor customers," said Michael Decker, senior vice president for research and public policy at Bond Dealers of America.

Decker points out that the statement "really focuses on ensuring that both sides of the transaction understand the risks associated with being involved in a Libor transaction, given that it appears Libor is going away pretty soon."

According to the staff statement, "understanding the potential risks, rewards, and costs is especially important when recommending Libor-linked securities."

The statement also highlights specific considerations for underwriters of primary offerings of municipal securities and those for broker-dealers making recommendations of municipal securities.

For example, SEC staff believe that it would be difficult for a broker-dealer to satisfy its duty of care to customers in a situation where the broker-dealer recommends a Libor-linked security without fallback language.

Fallback language specifies a process for identifying a replacement rate in the event that a benchmark rate is not available.

Essentially, the SEC sees the replacement rate for a Libor-linked security as a factor that generally should be considered as part of a recommendation.

Decker said that while fallback provisions were originally conceived for temporary instances where the Libor wouldn't be published for a short period of time, the provisions have now become more robust.

"They account for the notion that Libor may go away entirely and specify a more practical and workable kind of long-term solution," Decker said.

For example, Decker pointed out that instead of merely specifying the prime rate for some period of time, a Libor-transition fallback provision would specify the SIFMA index or some alternative index that the issuer and other parties to the transaction could use.

Regarding municipal securities underwriting, the SEC staff statement pointed to prior SEC staff

guidance and guidance from the Municipal Securities Rulemaking Board concerning fair dealing requirements under MSRB Rule G-17.

The Office of Municipal Securities staff noted that "broker-dealers should consider the impact that the Libor transition may have in connection with other duties" including suitability standards in MSRB Rule G19 and disclosure rules under MSRB Rule G-47.

The SEC staff statement also reminds funds and advisors to monitor and manage conflicts of interest associated with the Libor transition.

Les Jacobowitz, a partner at Arent Fox, LLP who has extensive experience representing issuers, borrowers, underwriters, and financial institutions, has been writing about the Libor transition for a couple of years.

"As the UK FCA and U.S. regulators admonish, everyone should act now to slowUSD LIBOR use for the next four weeks through the year-end Libor/SOFR [Secured Overnight Financing Rate] transition deadline," Jacobowitz wrote Dec. 1.

Jacobowitz also noted that slowing of Libor use was "a recommendation and not a requirement."

However, with a nod to the classic movie, Casablanca, Jacobowitz says he is, "shocked, shocked" that Libor-linked instruments are still being recommended by underwriters and financial advisors.

"I can't believe issuers and conduit borrowers are still entering into Libor-based instruments, especially those that terminate after USD LIBOR goes away [in June 2023]," Jacobowitz explained.

Meanwhile, with respect to both interest rate swaps and floating rate notes, Decker is seeing notable movement away from Libor.

"There may be some new transactions that are still priced off of Libor, but it's my understanding that those are becoming rarer and rarer," Decker said.

Overall, Decker believes that underwriters, municipal advisors, and sales reps should be clear in their disclosure with customers and clients about Libor going away and about specifics of a transaction.

"In that sense, we agree with the SEC that disclosure and transparency are important," Decker said.

The Bond Buyer

By Kelley R. Taylor

December 08, 2021, 1:06 p.m. EST

SEC Staff Statement on LIBOR Transition - Key Considerations for Market Participants.

Read the SEC Staff Statement.

Staff of the U.S. Securities and Exchange Commission

Dec. 7, 2021

SEC Staff Issues Key Considerations on LIBOR Transition: Latham & Watkins

As a major LIBOR transition milestone approaches, a Staff Statement provides key considerations for market participants regarding their obligations.

On December 7, 2021, the Staff of the Securities and Exchange Commission (SEC) issued a statement (the Statement) on the transition away from the London Interbank Offered Rate (LIBOR). The transition away from LIBOR is reaching an inflection point as the publication of the USD LIBOR benchmark for the 1-week and 2-month USD LIBOR maturities and many non-USD LIBOR maturities cease immediately after December 31, 2021.[1] The SEC, like other regulators around the world, continues to emphasize its expectation that market participants understand the risks associated with LIBOR transition and take appropriate action to move to alternative rates in a manner that protects customers, counterparties, the firm itself, and the capital markets more broadly.

The Statement provides guidance for broker-dealers and registered investment advisers as they approach the imminent transition away from LIBOR, highlighting as part of conduct risk their duties under Regulation Best Interest (Reg. BI) as well as fiduciary obligations under the US securities laws. Specifically, the Statement includes timely reminders for:

- Broker-dealers recommending LIBOR-linked securities
- Broker-dealers underwriting or recommending municipal securities
- Investment advisers recommending LIBOR-linked securities
- Funds and investment advisers investing in LIBOR-linked securities
- Companies and issuers of asset-backed securities making disclosures related to the LIBOR transition

Obligations for Broker-Dealers Under Reg. BI

According to the Statement, broker-dealers should be mindful of their obligations under Reg. BI when recommending LIBOR-linked securities to retail customers. Under Reg. BI's Duty of Care, "a broker-dealer must exercise reasonable diligence, care, and skill to, among other things, understand the potential risks, rewards, and costs associated with the recommendation."

In the Statement, SEC Staff emphasized that based on a fact-specific analysis broker-dealers must have a reasonable basis to believe that any recommendation they make involving LIBOR-linked securities is in their retail customers' best interests. According to SEC Staff, "reasonable diligence" may take into account client investment objectives, as well as the characteristics of the underlying securities such as complexity, risks, rewards, costs, liquidity, volatility, likely performance, expected return, associated incentives, etc.

The Statement clarifies that, to meet the Reg. BI Standard, broker-dealers must confirm whether a security has robust fallback language in its offering documents that clearly defines an alternative reference rate (ARR) to LIBOR. If a security does not have robust fallback language, then the recommendation must be "premised on a specific, identified, short-term trading objective." In contrast, if a security does have robust fallback language, the broker-dealer must assess the impact the replacement rate will have on the expected performance of the security to determine whether the security is still in the customer's best interest.

Furthermore, under Reg. BI, broker-dealers that have agreed to perform monitoring services for a retail customer must reassess the potential risks, rewards, and costs of any LIBOR-linked security in their retail customer's account to ensure the investment is still in the customer's best interests. This obligation applies to buy, sell, or hold recommendations, and even when a broker-dealer remains silent (i.e., an implicit hold recommendation).

Obligations for Broker-Dealers Related to Municipal Securities

In addition to the Reg. BI standard for recommendations to retail customers, broker-dealers are subject to a few additional rules when recommending LIBOR-linked municipal securities.

1. Exchange Act Rule 15c2-12 requires broker-dealers to obtain and review a "deemed final" official statement by a municipal obligor. Per this rule, underwriters must have a reasonable basis to believe the key representations in the "deemed final" official statement are true. To meet this "reasonable basis" standard, broker-dealers underwriting municipal securities should review the municipal obligor's exposure to LIBOR-transition risks to ensure those risks are adequately addressed in the obligor's key representations.
2. Broker-dealers making recommendations to non-retail customers are subject to the suitability standard in MSRB Rule G-19. Accordingly, broker-dealers should consider a municipal obligor's exposure to LIBOR transition risks when making a suitability determination.
3. When broker-dealers sell or purchase municipal securities, MSRB Rule G-47 requires they disclose material information known or available to established industry sources regarding the municipal obligor's exposure to LIBOR transition risks.

Obligations for Registered Investment Advisers and Registered Funds

SEC-registered investment advisers must consider their fiduciary obligations under the Investment Advisers Act of 1940 when recommending LIBOR-linked securities and investment strategies. These fiduciary principles require advisers to consider whether LIBOR-linked investments are consistent with their client's goals. To do this, advisers must consider whether the investments or related contracts have robust fallback language providing a clear ARR. When an investment does include an ARR, advisers should consider whether those rates will cause the investment to depart from their client's goals or risk tolerance.

Funds and advisers should monitor and manage conflicts arising from the LIBOR transition. Specifically, advisers should make disclosures when the LIBOR transition impacts performance fees, which is likely for performance fees subject to a "hurdle rate" (the minimum return necessary for the adviser to start collecting the performance fee) that is tied to LIBOR.

LIBOR transition also implicates disclosure obligations for registered investment companies and business development companies to prevent misleading investors. Disclosures in offering documents for registered products must address the principal risks associated with the fund, including those related to the anticipated impact of LIBOR transition, if a fund invests a significant portion of its assets in LIBOR-linked investments.

Funds and advisers should also consider the impact the transition will have on valuation measurements that use LIBOR as an input, as well as the operational complexities that the LIBOR transition will introduce on their IT systems.

Obligations for Public Companies and Asset-Backed Securities Issuers

According to the Statement, public companies and asset-backed securities issuers should provide

meaningful insight to investors about the status of their efforts to address LIBOR transition risks. Specifically, companies should provide material and specific qualitative and quantitative information to investors, "rather than general statements about the progress of the company's transition efforts to date." To aid these disclosure requirements, the Statement outlines several specific disclosure recommendations:

- Companies should generally disclose the steps they have taken to identify their LIBOR exposure, what the company has done thus far to mitigate LIBOR transition risks, and what steps remain to mitigate those risks.
- Companies with outstanding debt that lacks robust fallback provisions should disclose how much LIBOR-linked debt they will have outstanding after the cession date and the steps the company is taking to mitigate the risks involved.
- Companies that include disclosures about the LIBOR transition in response to more than one disclosure requirement within a single filing should provide cross-references or otherwise connect the information to clarify for the investor the company's LIBOR risk profile.
- Firms specifically subject to regulatory guidance (such as the joint statements issued by the Board of Governors of the Federal Reserve System, the Office of the Comptroller of the Currency, and the Federal Deposit Insurance Corporation; and the Federal Reserve Board backed Alternative Reference Rates Committee) recommending that they avoid entering into new contracts that reference LIBOR after December 31, 2021, should disclose the details of their transition efforts and the impact of these efforts on their company, in alignment with such guidance.

Key Takeaways

The Statement's recommendations will be of particular interest to firms and individuals under the SEC's remit, as they may be indicative of the Staff's key regulatory and examination priorities. Since at least June 18, 2020, the SEC's Division of Examinations has highlighted that LIBOR transition is a priority, including when it issued a Risk Alert on LIBOR transition preparedness (see this Latham post for more information). As the long-anticipated deadline for key LIBOR tenors approaches, regulated firms should be alert to their various disclosure obligations and obligations under the fiduciary rules and Reg. BI. Firms should prepare for compliance with these rules, specifically as they relate to LIBOR transition.

Latham & Watkins LLP – Laura N. Ferrell, Marlon Q. Paz, Zach Lippman and Deric M. Behar

December 10 2021

MSRB RFC: ESG-Related Disclosure and ESG Labeling

Share Your Perspective on ESG Practices in the Muni Market

Read the MSRB's request for information on ESG-related disclosure and ESG labeling, and submit your comments
by March 8, 2022.

December 8, 2021

MSRB Requests Information on ESG Practices: Cadwalader

The MSRB issued a Request for Information on environmental, social and governance ("ESG") practices in the municipal securities market. MSRB is seeking information on (i) the disclosure of related risk factors and practices, and (ii) the labeling and marketing of municipal securities with ESG designations. Responses must be submitted by March 8, 2022.

Specifically, MSRB is asking the following questions:

Municipal Issuers:

- Are you currently providing ESG disclosures or information beyond what is legally required in your offering documents?
- Do you believe that the information in the ESG disclosures should be standardized?

Investors in Municipal Securities:

- Do you consider ESG information material to your investment decision?
- Do you have access to ESG-related information to make an informed investment decision?

Dealers:

- Does underwriting ESG-labeled bonds create any novel compliance issues? How might that differ between a primary offering and purchase or sale in the secondary market?

Municipal Advisors:

- Does the formulation and delivery of advice for ESG-related bonds and ESG-related disclosures raise any novel compliance challenges?

All Municipal Market Participants:

- Are there any ESG factors that could pose a systematic risk to the municipal market?
- There are organizations that have established voluntary standards; do those standards provide adequate guidance and transparency for investors?

Cadwalader Wickersham & Taft LLP

December 8 2021

MSRB Extends Comment Deadline on Draft Compliance Resources for New Issue Pricing: Cadwalader

The MSRB extended the deadline for comments on draft compliance resources related to new issue pricing. The comment deadline was extended from January 4, 2022 to January 19, 2022.

As previously covered, one proposed compliance resource would focus on underwriting activity under MSRB Rule G-17 ("Conduct of Municipal Securities and Municipal Advisory Activities") and supervisory obligations under MSRB Rule G-27 ("Supervision"). The second resource would focus on duty of care obligations under MSRB Rule G-42 ("Duties of Non-Solicitor Municipal Advisors") and

non-solicitor municipal advisors' duties under MSRB Rule G-44 ("Supervisory and Compliance Obligations of Municipal Advisors").

Cadwalader Wickersham & Taft LLP

December 7 2021

SEC Charges Adviser with Section 204A Violation for Failing to Maintain MNPI Procedures: Paul Hastings

Recently, the SEC settled an enforcement action against a registered investment adviser (the "Adviser") for allegedly failing to implement policies and procedures reasonably designed to prevent the misuse of material non-public information ("MNPI") in violation of Section 204A of the Investment Advisers Act of 1940 ("Section 204A"). The terms of the settlement required the Adviser to pay an $18 million penalty. Although the SEC's pursuit of violations of Section 204A is nothing new, this action is significant for a couple of reasons.

First, the SEC's allegations focused on policies and procedures governing advisory personnel who were considered "above-the-wall" in relation to the Adviser's MNPI informational barriers. Specifically, although the Adviser had instituted walls that prohibited certain personnel from obtaining MNPI from the Adviser's affiliates, the Adviser allegedly had no procedures or "walls" that governed senior personnel who sat on the Adviser's Investments Committee (i.e., in a position above the informational walls) and ratified investment decisions for the Adviser. Those senior individuals also allegedly "had access to" MNPI about many of the issuers in which the Adviser invested through their work as consultants acting on behalf of the Adviser's affiliates.

Second, the SEC's allegations suggest that the agency is willing to take an aggressive view when determining what type of information might constitute MNPI for the purpose of Section 204A. Here, the SEC classified information relating to the Adviser's internal investment strategies and allocations as "MNPI" for the purposes of Section 204A. In other words, the SEC considered the procedures the Adviser had in place to prevent the misuse of information relating to the Adviser's own investment holdings and allocations in determining whether the Adviser's policies were adequate under Section 204A. Traditionally, the SEC has not designated this type of information as MNPI for the purposes of Section 204A. Further, some of the information at issue related to municipal debt securities, which are rarely, if ever, the subject of SEC insider trading claims.

Background: Senior Advisory Personnel Wore Many Hats and Sat Above the "Wall"

According to the SEC, the Adviser invested the vast majority of its funds indirectly through third-party investment managers who maintained discretion over the funds. Some of these indirect investments were held in separately managed accounts ("SMAs"). The SEC alleged that the Adviser was aware of the SMAs' holdings and activity because the Adviser maintained books and records of all trades executed by the third-party managers in the SMAs. The SEC also alleged that the Adviser had insight into certain details regarding the holdings in the remaining portion of the indirect investments because the Adviser had access to, among other things, client updates that it received from the third-party managers.

The SEC alleged that the Adviser managed the money of the partners and personnel of the Adviser's parent company ("Parent"), a large consulting company. To help manage the money, the Adviser

apparently formed an Investments Committee that was responsible for overseeing and monitoring all investments. The Investments Committee was allegedly responsible for ratifying or approving investment decisions, including planned allocations to third-party managers. The SEC alleged that members of the Adviser's Investments Committee also separately provided consulting services to public companies and entities emerging from bankruptcy on behalf of the Parent.

Among other things, the SEC alleged that the Adviser invested hundreds of millions of dollars in the securities of issuers about which members of the Investments Committee had access to substantial MNPI as a result of the consulting services that those individuals performed on behalf of the Parent. For example, the SEC alleged that the Adviser's Investments Committee allocated millions of dollars in investments to a third-party manager that substantially invested in a public company ("Company A "). The SEC alleged that, at the same time, a member of the Investments Committee was responsible for overseeing the strategic and corporate advice that the Parent was then providing to Company A. The SEC indicated that, given this type of conduct, the "risk of misuse of MNPI was real and significant."

The SEC alleged that the Adviser did not have policies and procedures to address this risk and prevent the misuse of MNPI to which members of the Investments Committee had access.

SEC Classifies the Adviser's Internal Investment Decisions as "MNPI"

The SEC also alleged that the Adviser lacked policies and procedures to prevent the misuse of MNPI relating to the Adviser's own internal investment decisions. Specifically, the SEC alleged that members of the Investments Committee were "aware of MNPI regarding [the Adviser's] investment strategies, concentration limits, risk limits, and third-party managers allocations, and had access to [the Adviser's] holdings," including holdings of securities that are very infrequently the subject of SEC insider trading claims, such as municipal bonds and private senior secured debt for an issuer in bankruptcy proceedings.

The SEC claimed that, armed with this MNPI regarding the Adviser's investment positions, members of the Investments Committee might be tempted to engage in conduct designed to influence those investments. For example, the SEC suggested that members of the Investments Committee might influence their consulting advice in a way that favored the Adviser's investments, given the overlap between the issuers for which the members of the Investments Committee provided consulting services and the issuers in which the third-party managers made investments. Notably, the SEC did not allege that any of the members of the Investments Committee actually tried to influence the investment decisions in an improper way. Nonetheless, the SEC alleged that the Adviser did not have policies and procedures in place to prevent the misuse of this "MNPI."

The Takeaways

This action presents many takeaways and reminders for registered broker-dealers and investment advisers:

- A violation of Section 204A does not require an allegation of insider trading
- According to the SEC, a "risk" of misuse of MNPI is sufficient to substantiate a finding that policies and procedures are not reasonably designed
- From the SEC's perspective, a potential violation of Section 204A may be predicated on an individual merely having "access to" MNPI
- The SEC might allege that MNPI includes internal advisory decisions regarding a potential investment, which might significantly complicate an adviser's/broker-dealer's efforts to design procedures to prevent the misuse of MNPI under the federal securities laws

- "Above-the-wall" procedures must be considered when implementing informational barriers to prevent the misuse of MNPI
- Wearing many hats can lead to complex issues regarding MNPI policies and procedures under Section 204A

Paul Hastings LLP – Thomas A. Zaccaro , Nick Morgan, John P. Nowak and Jessica Baker

December 2 2021

Pre-Order the New Electronic GAAFR.

Highlights of the new eGAAFR:

Updated to incorporate all new authoritative guidance through GASB Statement No. 97, and GASB's Implementation Guide updates through June 30, 2021.

Enhanced anticipation notes (RANs, TANs, and BANs) discussion in Chapter 12 – Asset and Liability Recognition and Measurement in Governmental Funds and added Illustrative journal entries for issuance and refunding of bond anticipation note.

Revamped Chapter 20 – Postemployment Benefits:

- Topics reorganized to reflect the various types of postemployment benefit plans.
- Relocated and expanded note disclosure content to include all requirements for all types of trusted defined benefit plans, all non-trusted defined benefit and defined contribution plans, and nonemployer contributors.
- Added accounting and financial reporting for nongovernmental cost-sharing pension plans.

Added a new Chapter 27, with expanded discussion of accounting for leases, PPPs, and SBITAs, including determining the terms (length) of the agreements and measuring assets, liabilities, deferred inflows and outflows of resources, and inflows and outflows of resources recognized for each type of arrangement.

Incorporated detailed note disclosure requirements for:

- Subscription-based information technology arrangements (SBITAs)
- Public-private and public-public partnerships (PPPs) and availability payment arrangements (APAs)
- In-substance defeasances of debt using only existing resources, and
- Minority-share asset retirement obligations.

Expanded discussion of note disclosure and actuarial section requirements for reporting by pension and OPEB plans.

Provided guidance for governments transitioning their reference rate(s) from an interbank offering rate, including LIBOR based on GASB Statement No. 93.

PRE-ORDER TODAY!

The new electronic *GAAFR* has been updated to incorporate all new authoritative guidance through GASB Statement No. 97, and GASB's Implementation Guide updates through June 30, 2021, and much more. Note: All current *GAAFR Plus* subscribers will receive the publication as part of their

subscription. Not a *GAAFR Plus* subscriber? Pre-order by December 31 and receive a four-month trial to *GAAFR Plus*.

SEC Names New Acting Director of the Office of Municipal Securities.

The Securities and Exchange Commission (SEC) named Ernesto Lanza as its acting director of the Office of Municipal Securities (OMS).

Lanza replaces Rebecca Olsen, who was named deputy chief for the Division of Enforcement's Public Finance Abuse (PFA) Unit. Mark Zehner, who held the PFA role since July 2010, is retiring from the agency after 25 years of service.

"I look forward to working closely with Ernie on oversight of municipal securities," SEC Chair Gary Gensler said. "This critical $4 trillion market finances local governments and the essential infrastructure of our communities, such as roads, hospitals, and schools. I thank Rebecca for her leadership of OMS since 2018 and congratulate Mark on his retirement from the SEC."

Lanza has served as senior counsel to the OMS director since 2019. Before that, Lanza was in private practice focusing on public finance matters related to securities law, disclosure, and market structure issues. Previously, he served as the deputy executive director of the Municipal Securities Rulemaking Board (MSRB), where he led several policy initiatives, including the launch of the EMMA system. Prior to that, Lanza was the MSRB's chief legal officer and general counsel. He holds a J.D. from the University of Pennsylvania Law School and earned his undergraduate degree cum laude from Harvard University.

Olsen became head of OMS in September 2018. She previously served as the deputy director, chief counsel, and attorney fellow in the office. She earned a bachelor's degree from Boston College, a J.D. from the Georgetown University Law Center, and an LL.M in International Business Law from the Vrije Universiteit Amsterdam, The Netherlands.

Zehner joined the SEC in January 1997. Before joining the Enforcement Division, he served as Regional Municipal Securities Counsel in the SEC's Philadelphia Regional Office and as an attorney-fellow in OMS. Zehner received a J.D. from the University of Pennsylvania Law School and a B.A. from Dartmouth College. He won the Stanley Sporkin Award in 2006, the agency's highest honor for enforcement staff.

FINANCIAL REGULATION NEWS

BY DAVE KOVALESKI | DECEMBER 7, 2021

Retired SEC Enforcer Zehner Reflects on Landmark Muni Cases.

Mark Zehner spent 25 years dropping the hammer on municipal securities wrongdoers, helping to firmly establish the Securities and Exchange Commission's enforcement of the laws in the muni market.

His career saw the SEC bring cases against negligent issuers and audacious fraudsters, broker-

dealers and bond lawyers. He still views the municipal market as a place populated overwhelmingly by good people.

“Fundamentally, the vast majority of muni issuers are trying to do the right thing,” Zehner said. “The vast majority of underwriters and municipal advisors are trying to do the right thing.”

Zehner, 62, retired as the deputy chief of the SEC’s public finance abuse unit at the end of November. He talks quickly and laughs easily, but there’s no mistaking how seriously he has taken the work to which he devoted the majority of his professional life. He can recall the details of cases dating back 15 or more years, and he speaks about them with clear conviction.

“We call ’em like we see ’em,” he said.

Zehner began his SEC tenure in 1997 as an attorney fellow in the SEC?s Office of Municipal Securities, where he got a taste of the life of an enforcer through examining the yield-burning scandal of the 1990s. Working in Washington, D.C., but maintaining his home in Philadelphia, Zehner commuted to and from work by train daily before finding a home in the SEC’s Philadelphia office.

Zehner’s career as an enforcer spans a number of landmark cases that created precedents in municipal securities enforcement. In a phone interview shortly after his retirement, Zehner discussed a number of those cases and offered some thoughts on the future.

The first cases Zehner named as significant were two that he said served as a sort of announcement the SEC wouldn’t hesitate to bring charges in the municipal bond space.

The SEC’s 2004 action against the Dauphin County, Pennsylvania General Authority saw the commission charge the issuer for failing to disclose to potential bondholders that the tenant responsible for more than half of the parking revenues backing its 1998 bonds had already planned to leave that space at the time the bonds were issued. The SEC found this was material to would-be purchasers of the bonds, and should have been included in the official statement.

Around the same time, the SEC also announced an administrative action against broker-dealer L. Andrew Shupe and bond lawyer Ira Weiss for alleged violations of the antifraud provisions of the federal securities laws in connection with a June 2000 offering of tax-exempt notes by the Neshannock Township School District, located in Lawrence County, Pennsylvania.

The SEC found that the true purpose of the offering was a scheme by underwriter Shupe to secure $ 225,000 dollars of arbitrage profits by investing the proceeds for three years without spending them on capital projects, even though the tax-exempt status of the bonds depended on the authority reasonably expecting to spend down the proceeds in that time. The SEC further alleged that Weiss also committed fraud by nonetheless rendering an unqualified opinion the notes were tax-exempt and that nothing had come to his attention to lead him to believe the offering documents were inaccurate.

The case against Weiss became a months-long affair of appeals, eventually ending with the SEC’s triumph in the U.S. Court of Appeals for the District of Columbia.

These cases served as an announcement of the SEC’s readiness to act when it saw cause, Zehner said, while other cases established still more precedents.

Perhaps no enforcement pursuit of Zehner’s career created quite as much of a muni market splash as the Municipalities Continuing Disclosure Cooperation Initiative, or MCDC. Launched in March

2014, the MCDC promised underwriters and issuers lenient settlements if they self-reported instances where issuers falsely said in offering documents they were in compliance with their continuing disclosure agreements.

The initiative was the brainchild of then-SEC enforcement lawyer Peter Chan, who is now in private practice. But Zehner said the MCDC, like all of the muni actions of the past decade, was a triumph of the work of the whole public finance abuse unit.

“That was an incredible team effort,” Zehner said.

The MCDC inspired fierce debate among issuer officials and bond lawyers, some of whom accused the SEC of being too aggressive in targeting issuers. In total, the initiative led to settlements with 72 issuers from 45 states. In addition, 72 underwriters representing 96% of the underwriting market by volume paid a total of $18 million of MCDC settlements.

Zehner said he believes the MCDC, which wrapped up in late 2016, had a positive impact on issuer disclosure practices in the short term. But it remains to be seen whether that will stick, he said.

Zehner said looking forward, one might do well to examine the SEC’s orders suspending two former KPMG auditors who approved and authorized the issuance of an unmodified audit opinion on The College of New Rochelle?s fiscal year 2015 financial statements, despite not having completed critical audit steps and having been given information that raised serious red flags.

The school’s controller had already faced SEC fraud charges for overstating the financial position of the now-defunct school. Bond lawyers said the KPMG cases were important, because the action showed that the SEC would hold professionals like auditors accountable for negligence even if they weren’t complicit in underlying fraud.

“I think we will see more accounting cases going forward,” Zehner predicted.

Zehner was complimentary of both the unit chiefs he served under since the SEC announced the creation of its specialized enforcement units, including what is now the public finance abuse unit, in 2010. Elaine Greenberg led the unit until 2013 when she left to enter private practice, and the unit has since been led by LeeAnn Gaunt.

Zehner’s place as deputy chief has been filled by Rebecca Olsen, who had until recently been director of the Office of Municipal Securities.

As described by him, Zehner’s future holds a break from the intellectual challenge of securities law. He said he wants to travel and devote more time to his work in the Catholic Church. Much of Zehner’s work is through the Saint Vincent De Paul Society, a nearly 200-year old society dedicated to providing help to the needy.

By Kyle Glazier

BY SOURCEMEDIA | MUNICIPAL | 12/09/21 09:03 AM EST

Ernesto A. Lanza Named Acting Director of SEC Office of Municipal Securities.

Washington, D.C.–(Newsfile Corp. – December 3, 2021) – The Securities and Exchange Commission today announced that Ernesto A. Lanza will serve as Acting Director of the Office of Municipal

Securities (OMS). Mr. Lanza, who has served as Senior Counsel to the OMS Director since 2019, replaces Rebecca J. Olsen, who was named Deputy Chief for the Division of Enforcements Public Finance Abuse (PFA) Unit. Mark R. Zehner, who held the PFA role since July 2010, is retiring from the agency after 25 years of service.

“I look forward to working closely with Ernie on oversight of municipal securities,” said SEC Chair Gary Gensler. “This critical $4 trillion market finances local governments and the essential infrastructure of our communities, such as roads, hospitals, and schools. I thank Rebecca for her leadership of OMS since 2018 and congratulate Mark on his retirement from the SEC.”

Prior to joining the SEC in 2019, Mr. Lanza was in private practice with a focus on public finance matters related to securities law, disclosure, and market structure issues. He previously served as the Deputy Executive Director of the Municipal Securities Rulemaking Board (MSRB), where he led a number of policy initiatives, including the launch of the EMMA system. Before that, he was the MSRBs Chief Legal Officer and General Counsel. Mr. Lanza holds a J.D. from the University of Pennsylvania Law School and earned his undergraduate degree cum laude from Harvard University.

Ms. Olsen became head of OMS in September 2018 and previously served as the Offices Deputy Director, Chief Counsel, and attorney fellow. She earned a bachelor’s degree from Boston College, a J.D. from the Georgetown University Law Center and an LL.M in International Business Law from the Vrije Universiteit Amsterdam, The Netherlands.

Mr. Zehner joined the SEC in January 1997. Prior to joining the Enforcement Division, he served as Regional Municipal Securities Counsel in the SECs Philadelphia Regional Office and as an Attorney-Fellow in OMS. He received a J.D. from the University of Pennsylvania Law School and a B.A. from Dartmouth College. In 2006, he received the Stanley Sporkin Award, the agencys highest honor for enforcement staff.

MSRB Staff Examines Change in Use of External Liquidity over Time: Cadwalader

In a new report, MSRB staff examined the use of external liquidity in both “small” ($100,000 or less) and “large” ($1,000,000 or more) secondary market transactions over the past decade. As defined in the report, external liquidity is when “a customer purchase or sale is filled using the offering or bid of a dealer that is different than and not affiliated with the client’s dealer.”

MSRB staff analyzed how municipal market participants accessed the secondary market of fixed--, long-term securities in the years 2011, 2015, 2019 and 2020. As to small market transactions, from 2011 to 2019, the staff found an increase in external liquidity likely due to the increased use of online brokerages largely by individual investors. (From 2019 to 2020, there was a minimal decrease in small market transactions, likely attributable to the pandemic.) As to large market transactions, the MSRB found a decrease in external liquidity from 2011 to 2019. The researchers identified an increase in large market transactions in 2020. The MSRB concluded that the pandemic had a large impact on external liquidity usage in 2020. The staff researchers found that external liquidity usage varied greatly from month to month, peaking at the beginning of the pandemic and declining throughout the year.

The study also found a consolidation and decrease in the number of providers of external liquidity over the period. (In 2020, the top ten external liquidity providers accounted for 45% of all liquidity in

trades, which was up from 42% in 2011). The MSRB suggested that those providers who left the market did not have a significant presence, and the number of firms providing "significant" external liquidity was on the rise.

MSRB staff said it will continue to monitor the use of external liquidity in the marketplace and will update the report when appropriate.

Cadwalader Wickersham & Taft LLP

November 19 2021

Quarterly Report of the GASB Chair.

The GASB Chair reports quarterly on the activities of the GASB to the Financial Accounting Foundation Board of Trustees and the members of the Governmental Accounting Standards Advisory Council.

January 1, 2021–March 31, 2021

Here's One Way to Get the Municipal Bond Market to Come Clean on Climate Change Risks.

The SEC might consider offering issuers a grace period before cracking down, this firm suggests

As climate change continues to take a toll on the built environment in the United States, investors are often in the dark about its effects. State and local governments, which issue roughly $500 billion of bonds each year, are being urged to be more proactive about addressing climate change, as MarketWatch has reported.

Now, a new proposal from a longtime muni-bond research firm offers a suggestion for regulators focused on climate risks and looking to encourage municipal issuers to be more upfront with buyers of their bonds.

The solution: "a Climate MCDC program that allows muni borrowers not making sufficient disclosure of their material credit vulnerabilities via climate change a short period to officially post the related information they possess," wrote analysts at Municipal Market Analytics in a Nov. 22 report.

MCDC stands for "Municipal Continuing Disclosure Cooperation," and it refers to a successful 2014 initiative of the U.S. Securities and Exchange Commission, which offered more favorable terms for any municipal bond issuer willing to voluntarily self-report earlier instances of being out of compliance with disclosure regulations.

As the Municipal Market Analytics report notes, "In the past month of the MCDC safe harbor window (December 2014), 30 municipal issuers filed their first notices of past technical (23) and monetary (7) defaults. Even considering the COVID-19 pandemic, December 2014 still holds the

record for most monthly new impairments since the Great Recession."

MMA President Thomas Doe has been vocal about his skepticism of the municipal bond market's approach to pricing climate-change risk. In a series of interviews with MarketWatch in August, he called migration to the sunshine states of the U.S. "denial": "you may be able to live there for a short period, but it's not going to be a 20-year experience."

Muni-bond defaults are scant: 0.10% compared to 2.25% of all corporate bonds, according to the Municipal Securities Rulemaking Board, but advocates of better disclosure, like Doe, say climate risk is very mispriced. It might take only one bad weather event and one Congress reluctant to keep bailing out states and locals for an issuer to have trouble paying its debts.

Few other public finance observers have been quite as hawkish, but many share some concern that state and local issuers aren't being as candid about the climate risks they face as investors might want — whether deliberately, or unintentionally.

The Nov. 22 note echoed much of what Doe told MarketWatch last summer: to the extent that the muni market needs discipline, it most likely won't come from investors, since market supply and demand are so out of whack.

"Investors urge issuers to disclose 'more and better information' about risks, but don't enforce true market discipline, the analysts wrote.

Yet, "Industry organizations representing issuers are encouraging voluntary disclosure with the hopes of avoiding a future regulatory mandate. But history suggests that efforts to obtain new voluntary disclosures may not generate the participation warranted and ultimately lead to a regulatory response."

MMA concludes its proposal by noting that there are plentiful, often free, tools for issuers to use to quantify their climate risk. The SEC would be well within its rights to review bond documents to see if they "adequately disclosed reasonably known material risks to investors;" and, more broadly, to "convey its disclosure expectations."

States are better-positioned to lead these efforts than local governments are, MMA writes, adding: "It is inefficient and not as credible for tens of thousands of local governments— varying in size, sophistication, and resources and many overlapping—to individually assess highly complex data, determine how their tax-bases, revenues, and operations could be impacted, develop resiliency plans, and make appropriate disclosures, all while fighting to retain or grow their respective allocations of local aid as their states decide what to pay for and where."

MarketWatch

By Andrea Riquier

Nov. 23, 2021

There Are No Municipal-Market Bond Vigilantes When It Comes To Climate Risk, This Study Confirms.

The old saw that municipal bonds don't default never accounted for climate change

From wildfires to floods, hurricanes to heat, the effects of climate change on our communities are well-known, and widely expected to get worse.

But as participants in the municipal debt market are starting to realize, there are no bond vigilantes to enforce discipline on state and local government issuers. A new study confirms that notion, showing that investors haven't yet begun to demand any premium for bonds that may be more at risk due to extreme weather.

That means that as weather becomes more volatile, things may have to change: either municipalities will pay more to borrow, or state governments and Washington may increasingly pick up the tab to make bondholders whole.

The report, from climate analytics firm risQ, Inc. analyzed the yields on about 800,000 municipal bonds issued between 2006 and 2021, accounting for about $2.5 trillion of the $3.9 trillion outstanding. "This is an era," the report notes, "where it is reasonable to assume climate risk was broadly recognized as a potential issue."

The research process involved making an estimate of the expected yield of all the bonds in the data set, based on factors that are known to influence yield, such as duration of the bond, type of issuer, and so on. It omitted climate risk as an input. Then, the researchers layered a proprietary climate risk score over the bonds, demonstrating that there is no correlation between climate and any additional risk premia for bonds that was unexplained by the other drivers.

The researchers then reran the same model, using only bonds issued between 2017 and 2021, noting that "physical climate risk came to the forefront of the collective awareness of the market after 2017's hurricane season," which remains the costliest on record.

But they come to the same conclusion with the second experiment: climate doesn't influence yields.

In addition to the data analysis they perform, risQ analysts have some important takeaways about why the municipal market hasn't yet reckoned with climate risk.

Among them is the old saw that muni bonds rarely default. As they note, "compared to other asset classes, municipal bonds have indeed been historically less risky. Because of this, systemic risk in general (climate and otherwise) has not been nearly as central a concern to the world and culture of municipal bonds as it has been to insurance or mortgage-backed security markets."

Another is a belief that climate hasn't historically caused defaults, an argument "that we hear less and less of as the climate crisis worsens," the report notes. They call climate risk "a 'frog in a pot of boiling water' situation, wherein systemic risk is significantly underestimated, and the heat will at least turn up gradually, and maybe abruptly."

What does this mean for investors?

Among other things, risQ repeats some of the themes MarketWatch has reported on in recent months: investors should be aware that the municipal market may have risks that are camouflaged by lopsided supply and demand, issuers with little incentive (so far) to disclose their challenges, and ratings firms and regulatory agencies that may not be as proactive as necessary.

The risQ report concludes with one example of a recent climate catastrophe: the fire in Paradise, California, in 2018, where nearly 90% of the town was destroyed and 90% of the population forced to leave. Despite that, Paradise was able to pay its bondholders, both because of state legislation that allowed California to step in and backfill payments, and because the state was able to secure

direct federal aid.

As MarketWatch has previously reported, some observers think the municipal market may not be able to continue to rely on state and federal bailouts, particularly as “hundred year” weather events become every-year occurrences. By the time the frog realizes he’s in hot water, in other words, it may be too late.

“Bond issuers will need to prepare for potential ‘sticker shock’ in many cases — yields don’t reflect climate risk yet, but this is almost certainly a matter of when, not if,” risQ writes. But the sooner they take proactive steps, the better: addressing the problem is not just good for the overall market, but is considered a “credit positive” as well.

MarketWatch

By Andrea Riquier

Nov. 24, 2021

Implementing the Recommendations of the Task Force on Climate-Related Financial Disclosures (2021)

The 2021 TCFD “Annex” updates and supersedes the 2017 version of “Implementing the Recommendations of the TCFD.” It provides both general and sector-specific guidance on implementing the Task Force’s disclosure recommendations.

Download report

Increased Investor & Rating Agency Interest in Cybersecurity and Climate Change Disclosure in Municipal Bond Issuances.

The topics of ***Cybersecurity*** and ***Climate Change*** disclosure are generating increased investor and rating agency interest in municipal bond issuances. The Securities and Exchange Commission (SEC) has expressed concerns about the adequacy of such disclosure given the increased frequency of cybersecurity breaches and severe weather-related events and their impact on municipalities’ operations. SEC Release on Cybersecurity Disclosure; SEC Statement on Climate-Related Disclosure. Risks related to cybersecurity and climate change may be material to potential investors, and therefore, should be disclosed in bond offering documents.

Cybersecurity

Municipalities, like many other public and private entities, rely heavily on technology to conduct their operations, and as a result, are vulnerable to cyber threats. Yet, many municipal issuers fail to disclose these risks when they could have a material impact on operations due to, among other factors:

- a misunderstanding of the cyber issues by the individuals preparing the disclosures;
- the need to protect and keep private the mitigation measures; or

- uncertainty surrounding the potential impact of the cyber threats.

Lack of disclosure, however, will leave investors wondering whether there have been any threats or attacks and whether any mitigation strategy against such attacks exists at all. Investors want to assess the adequacy of the disclosure for the level of risk and the nature and quality of the management capabilities and mitigation strategies of the issuer. Topics relative to cybersecurity disclosure should include:

- recent cyber-attacks, that did, or could have, a material effect on operations; and
- mitigation strategies against cyber-attacks such as, insurance to protect against such attacks, upgrades to software and policies and committees put in place relating to the security of the network.

Climate Change

While the impacts of climate change have received media attention for many years, consideration of climate change in disclosure documents is a relatively new and evolving expectation. Earlier this year, the SEC created a Climate and Environmental Social Governance (ESG) Task Force to develop initiatives to identify climate and ESG disclosure related conduct. Given the SEC's heightened focus and that the increase in severe weather may impact state and local tax collections and increase infrastructure costs, municipal issuers should evaluate their current practice related to disclosure of climate risk to ensure that such risks are being vetted and disclosed. Specifically, municipalities should disclose:

- recent weather-related events that had an impact on operations;
- geographic location and what weather events it may be vulnerable to in light of the location such as flooding, wind and/or fires and their potential impact; and
- best practices for monitoring the ever-changing impacts of climate change and any plan for disclosure of such risks for future issuances.

Municipal issuers should consult with the professionals that assist them with their offering documents, including their municipal advisors and disclosure counsel, if any, to ensure that such offering documents include adequate cybersecurity and climate change disclosure.

Pullman & Comley LLC

by Jessica Grossarth Kennedy

November 17, 2021

SEC's FY 2021 Enforcement was Robust in the Muni Arena.

The Securities and Exchange Commission's enforcement results for fiscal year 2021 highlight the SEC's focus on disclosure in the municipal finance space.

The results, released late Thursday, show the Commission overall filed 7% more enforcement actions in 2021 than in 2020. It also awarded over $564 million to more than 100 whistleblowers, surpassing $1 billion over the life of the SEC whistleblower program.

Twelve of the 697 SEC enforcement actions this year were categorized under public finance abuse.

That represented 2% of the total enforcement actions and is consistent with the 12 public finance abuse actions taken in the previous fiscal year.

Overall, of the total filed enforcement actions, 434 were new, 120 were against issuers for delinquent filings, and 143 were for follow-on administrative proceedings.

The SEC also obtained judgments for close to $2.4 billion in disgorgement, a more than 30% decrease from FY 2020. It also won over $1.4 billion in penalties, which represented a 33% increase over the previous fiscal year.

“As these results show, we go after misconduct wherever we find it in the financial system, holding individuals and companies accountable, without fear or favor, across the $100-plus trillion capital markets we oversee,? SEC Chair Gary Gensler said in a statement.

While total actions in 2021 decreased by 3% from 2020, the SEC said the new actions “spanned the entire securities waterfront,” and addressed what the Commission described as “traditional and emerging areas.”

For example, the SEC brought a number of first-of-their kind enforcement actions involving for example, so-called DeFi technology, the dark web, and regulation crowdfunding.

In the public finance abuse category, the SEC brought its first enforcement actions of Municipal Securities Rulemaking Board Rule G-42 regarding duties of municipal advisors, when it alleged that Choice Advisors LLC and two of its principals, Matthias, O’Meara, and Paula Permenter violated their fiduciary duties.

The agency found that O’Meara and Permenter entered into a prohibited fee-splitting arrangement with their former employer without disclosing either the arrangement or their relationship with the underwriting firm, to their clients.

The SEC further alleged that Choice, O’Meara, and Permenter unlawfully engaged in municipal advisory activities when they were not registered with the SEC or the MSRB.

Permenter agreed to settle with the SEC without admitting or denying any findings.

Beyond Rule G-42, the SEC brought several other public finance abuse enforcement actions in 2021.

For example, the Commission charged RBC Capital Markets and two individuals with unfair dealing in municipal bond offerings. According to the SEC, RBC allegedly improperly allocated bonds for institutional customers and dealers, who then resold or “flipped” the bonds to other broker-dealers at a profit. RBC agreed to pay more than $800,000 to resolve the charges without admitting or denying the SEC’s findings.

The SEC also charged a broker dealer and its former chief executive officer with failing to disclose a conflict of interest regarding a tender offer of municipal bonds and a school district and its former chief financial officer for allegedly misleading investors who purchased $28 million in municipal bonds.

Speaking at a National Association of Bond Lawyers workshop in October, Natalie Garner, senior counsel in the SEC’s public finance abuse unit, described issuer disclosure as “a major [enforcement] priority” and said that the SEC will make every effort to hold responsible “issuers who have engaged in fraud or who mislead investors.”

Garner also said that the enforcement actions taken in recent years highlight the importance of disclosure requirements.

Lily Becker, partner at Orrick, with an extensive background in government investigations and enforcement actions, echoed that notion. “I think we can expect a continued focus on both annual and periodic disclosures.” Becker said.

Becker explained that “because the SEC looks at both omissions and misstatements, entities should be thinking carefully about both including all material information and making sure information disclosed is accurate at the time of the disclosure.”

Securities lawyer Michael Botelho, partner with the Hartford, CT-based law firm of Updike, Kelly & Spellacy, acknowledged that enforcement activity in the municipal arena was fairly robust this past year.

“The SEC brought some high profile actions against municipal issuers and their key officials for inaccurate and incomplete disclosure and for misleading investors in their offering documents,” Botelho pointed out.

“Under the leadership of Chairman Gensler, I expect that the SEC will remain active in bringing new investigations and enforcement actions in this area and possibly exceed last year’s output,” Botelho said.

BY SOURCEMEDIA | 11/19/21

By Kelley R. Taylor

Hotel Builder Misled Municipal Bond Investors, Trustee Alleges.

- **Hard Rock Hotel developer lied about construction loan: UMB**
- **Bonds defaulted when wholesale lender failed to fund loan**

The developer of a planned Hard Rock Hotel in a suburb of Kansas City, Kansas, allegedly defrauded investors who bought about $23 million municipal bonds issued to help finance the project, according to a lawsuit filed in federal court.

Minnesota developer D. Jon Monson said that he had a $52 million construction loan in place when he sold the bonds, but hadn’t closed on that financing, which was only for $48.8 million, UMB Bank NA said in a Nov. 1 lawsuit filed in U.S. District Court in Kansas City. UMB is the trustee for the securities.

Monson was relying on a wholesale lender that in turn relied on third-party lines of credit to fund that loan, UMB said. The warehouse lender wasn’t able to fund the project, meaning the project couldn’t be completed and leaving no revenue to make required payments for the bonds, UMB said.

The developer also failed to contribute $3 million of the down payment deposit before the bonds were issued and “had no intention” of contributing $4.2 million for predevelopment costs and a $1.5 million equity payment, UMB alleged.

Monson didn’t immediately return a call seeking comment.

The developer won approval from the city of Edwardsville in 2018 to build the 241-room hotel and conference center near the Kansas Speedway, a NASCAR racetrack. Edwardsville issued tax-free debt in 2019 backed by the 4,500-person city's hotel tax and incremental increases in property taxes generated by the project.

The case is UMB Bank, NA v. D. Jon Monson; Compass Commodities Group III, LLC; 11 Water LLC, One10 Hotel HRKC LLC' and One10 Hotel Holding LL, 21-cv-2504, U.S. District Court, District of Kansas.

Bloomberg Markets

By Martin Z Braun

November 9, 2021, 1:43 PM PST

SEC Appoints New Director of Office of Credit Ratings: Cadwalader

The SEC named Ahmed Abonamah as its new Director of the Office of Credit Ratings. Mr. Abonamah had served as the Acting Director of the Office of Credit Ratings since October 2020.

Since joining the SEC in 2016, Mr. Abonamah has served in multiple roles within the SEC's Office of Municipal Securities, including as Deputy Director.

Cadwalader Wickersham & Taft LLP

November 9 2021

GASB Outlook E-Newsletter Fall 2021.

Read the GASB Newsletter.

MSRB Seeks Volunteers For Its FY 2022 Compliance Advisory Group.

The MSRB seeks volunteers for its FY 2022 Compliance Advisory Group! Associated persons of regulated entities serving in compliance, legal, trading, and operations; and public officials and employees of municipal entities are encouraged to volunteer.

Read more.

MSRB Reviews Initiatives under Strategic Plan: Cadwalader

At its quarterly Board of Directors meeting, the MSRB reviewed initiatives under the strategic plan for the municipal securities market (see previous coverage here).

The MSRB considered updates on:

- outreach to ensure municipal securities advisor principals are qualified with the Series 54 exam by November 30, 2021;
- the MSRB request for public comment on amendments to MSRB Rule G-27 (“Supervision”);
- implementation of new MSRB Form G-32 for filing primary market data;
- the Electronic Municipal Market Access website’s redesign; and
- environmental, social and governance considerations in the municipal market.

Cadwalader Wickersham & Taft LLP

October 29 2021

The Libor Transition: Protecting Consumers and Investors - SIFMA Statement

SUMMARY

SIFMA Statement for the Record submitted to the U.S. Senate Committee on Banking, Housing, and Urban Affairs on the November 2, 2021 Hearing titled: The Libor Transition: Protecting Consumers and Investors.

View the SIFMA Statement.

SIFMA Joint Letter to Senate Re Transition from LIBOR to Alternative Reference Rates.

SUMMARY

SIFMA in a joint letter with with other associations, provided comments to the United States Senate Committee on Banking, Housing, and Urban Affairs in support of federal legislation to address “tough legacy” contracts that currently reference LIBOR.

View the SIFMA Letter.

SIFMA signed with the following:

Structured Finance Association
Institute of International Bankers
Consumer Bankers Association
Bank Policy Institute
Commercial Real Estate Finance Council (CREFC)
U.S. Chamber of Commerce, Center for Capital Markets Competitiveness
Mortgage Bankers Association
Government Finance Officers Association
The Loan Syndications and Trading Association (LSTA)
The International Swaps and Derivatives Association (ISDA)
Student Loan Servicing Alliance

Housing Policy Council
The Financial Services Forum
Investment Company Institute
The Loan Syndications and Trading Association (LSTA)
The Real Estate Roundtable
American Bankers Association
The American Council of Life Insurers (ACLI)
National Association of Corporate Treasurers

MSRB Proposes Extension of Remote Inspection Relief: Cadwalader

The MSRB proposed to extend temporary relief for municipal securities dealers to conduct internal inspections remotely for calendar year 2022 until June 30, 2022. The MSRB stated that this extension is appropriate, given ongoing operational challenges due to the COVID-19 pandemic.

The proposed rule change to Supplementary Material .01 of MSRB Rule G-27 ("Supervision") would condition a dealer's election to conduct a remote inspection on:

- the dealer amending its written supervisory policies as appropriate;
- the dealer's use of remote inspections as part of an effective larger supervisory system; and
- maintenance of records related to remote inspections.

The MSRB filed the proposed rule change with the SEC for immediate effectiveness.

Cadwalader Wickersham & Taft LLP

October 27 2021

MSRB Holds First Quarterly Board Meeting of New Fiscal Year.

The municipal market's self-regulatory organization held its first quarterly Board of Directors meeting of Fiscal Year 2022 in Washington, DC, on October 27-28, 2021. The Municipal Securities Rulemaking Board (MSRB) discussed initiatives to advance the four goals outlined in its long-term strategic plan.

"Building on years of groundwork and investment in our people, our technology and our understanding of our diverse stakeholders' needs, the MSRB is poised to have one of the most productive and impactful years in our history," said MSRB Chair Patrick Brett. "This year, we are making meaningful strides to modernize municipal market regulation, provide transparency through technology, fuel innovation through data, and uphold the public trust."

Market Regulation

November is the final month of a 24-month grace period for municipal advisor principals to pass the MSRB's Series 54 professional qualification examination. The Board discussed the importance of continued outreach to municipal advisor firms to remind them of available resources and their obligation to ensure that any individual functioning in the capacity of a municipal advisor principal is

properly qualified with the Series 54 exam by the compliance deadline of November 30.

The Board also received an update on regulatory initiatives underway, including the ongoing review of the library of interpretive guidance in the MSRB rule book to identify pieces of guidance that should be clarified, amended or retired to facilitate compliance.

“As part of our commitment to prudent and practical regulation, we are focused on a retrospective review not just of the rules themselves but the over 200 pieces of associated guidance,” said MSRB Vice Chair Meredith Hathorn. “We will continue to make incremental but impactful progress toward reducing unnecessary compliance burdens on regulated entities and ensuring our rule book aligns with current market practices.”

The Board also received an update on regulatory initiatives authorized by the Board at previous meetings, including requesting public comment on potential amendments to modernize MSRB Rule G-27 on dealer supervision.

The Board discussed potential next steps to ease challenges raised by dealers related to the implementation of new MSRB Form G-32 for filing primary market data.

Market Transparency

The Board received an update on a six-month effort to reimagine the user experience and user interface of Electronic Municipal Market Access (EMMA®) website through collecting extensive input from a variety of stakeholders and producing future-state EMMA product design and functionality wireframes. This redesign will provide users with enhanced functionality and improve data quality and customization capabilities. While the complete overhaul of EMMA is a multi-year project, this most recent stakeholder input is already informing the creation of a roadmap for near-term enhancements, such as an improved feature to make it easier for issuers to ensure their disclosure filings are associated with all the necessary individual securities within the EMMA system.

“After years of behind the scenes work, we’re ready to start rolling out powerful new cloud-based tools on EMMA that will take the transparency of our market to a new level, and transform EMMA into a more dynamic and effective tool for informed decision-making,” Brett said.

Market Structure and Data

The Board discussed its data strategy and received a demonstration of a new master data management platform that will enhance the MSRB’s data governance and oversight capabilities. The Board also received an update on potential research topics to add to the MSRB’s growing library of market data analyses that shed light on trends and developments in market structure.

“Our strategic plan lays out an important focus on providing high quality market data that enables greater understanding of the market and empowers innovators to create data tools and services that serve the information needs of all market participants,” Brett said. “We are tremendously excited to invite our stakeholders to collaborate with us in test-driving data tools in our forthcoming EMMA Labs innovation hub.”

Public Trust

The Board discussed several topics that benefit from ongoing stakeholder engagement, including seeking information from the public about Environmental, Social and Governance (ESG) considerations in the municipal market; efforts to advance diversity, equity and inclusion in public finance; and a comprehensive review of the MSRB’s fee model as described in the Fiscal Year 2022

Budget.

“The Board appreciates hearing from market stakeholders, especially on an evolving market trend such as ESG that lends itself to many different perspectives,” Brett said. “We look forward to providing a forum for all interested stakeholders to share information and viewpoints on ESG considerations for the municipal market through our forthcoming public request for information.”

Date: October 29, 2021

Contact: Leah Szarek, Chief External Relations Officer
202-838-1300
lszarek@msrb.org

MSRB Announces Topics for Quarterly Board Meeting.

October 2021 Board of Directors Meeting Discussion Items

The Board of Directors of the Municipal Securities Rulemaking Board (MSRB) will meet October 27-28, 2021, in Washington, DC, for its first meeting of FY 2022, where it will discuss initiatives to advance the four goals outlined in its long-term strategic plan:

Market Regulation
The Board will receive an update on initiatives underway to modernize the rule book, including forthcoming requests for comment on draft MSRB Rule G-46 for solicitor municipal advisors and potential amendments to harmonize MSRB Rule G-27 on dealer supervision. Also in progress are regulatory filings to seek approval from the Securities and Exchange Commission (SEC) to modernize the text of MSRB Rule G-34 on obtaining CUSIP numbers and amend MSRB rules in light of SEC Regulation Best Interest.

The Board will receive an update on the implementation of new MSRB Form G-32 for filing primary market disclosures, as well as the Series 54 examination for municipal advisor principals.

Market Transparency
The Board continues its oversight of efforts to leverage cloud technology to modernize the MSRB’s critical market transparency systems, including the Electronic Municipal Market Access (EMMA®) website. The Board will receive an update on how input from stakeholders is advancing efforts to redesign the EMMA user interface and user experience.

Market Structure and Data
The Board will discuss its data strategy and receive a demonstration of a new master data management platform that will enhance the MSRB’s data governance and oversight capabilities. The Board also will discuss potential future research publications and initiatives to enhance understanding of trends and developments in market structure.

Public Trust
The Board will discuss several topics that benefit from ongoing stakeholder engagement, including seeking information from the public about Environmental, Social and Governance (ESG) considerations in the municipal market; efforts to advance diversity, equity and inclusion in public finance; and a comprehensive review of the MSRB’s fee model as described in the Fiscal Year 2022 Budget.

October GFOA Government Finance Review Available Now.

This month's GFR is now available to read electronically. Among the topics in the October edition is an in-depth look into interruptions at work with ideas to tame distractions to maximize workplace productivity.

READ ONLINE

GASB Changes Name of Report to "Annual Comprehensive Financial Report"

Norwalk, CT, October 19, 2021 — The Governmental Accounting Standards Board (GASB) today issued a pronouncement that changes the name of the most extensive report prepared following its standards to the annual comprehensive financial report or ACFR. Until now, the name applied to those reports was the comprehensive annual financial report.

The name change was prompted by GASB stakeholders raising concerns that the acronym of the prior name of the report sounds like a profoundly offensive term when spoken. The changes in the name and acronym were widely supported by individuals and stakeholder groups that responded to the April 2021 Exposure Draft proposing the changes.

Statement No. 98, *The Annual Comprehensive Financial Report*, establishes the annual comprehensive financial report and ACFR in generally accepted accounting principles (GAAP) for state and local governments and eliminates the prior name and acronym. Otherwise, no changes were made to the report's structure or content.

Regarding the issuance of Statement 98, GASB Chair Joel Black said, "Once this issue came to our attention, it was clear that working with our stakeholders to rename this important document was simply the right thing to do. Thank you to everyone who worked with us and shared their input."

Financial reports prepared following GAAP are required to contain basic financial statements (including notes to financial statements) and required supplementary information (such as management's discussion and analysis). Governments may voluntarily present those required components in an ACFR, which also contains more background and explanatory information from management, additional financial statements disaggregating certain columns in the basic financial statements, and a "statistical section" of 10-year trends in financial, economic, demographic, and operating information.

The requirements of Statement 98 are effective for fiscal years ending after December 15, 2021. Earlier application is encouraged.

The ABCs of ESG: Practical Considerations for Environmental, Social and Governance Disclosure in Municipal Finance.

In order to make an informed investment decision as to the purchase of municipal bonds, the latest trend is for investors to evaluate environmental, social and governance ("ESG") factors relative to the bond issuers in question, state and local governments.[1] In making this determination, investors

primarily look to the information provided by the issuers in the offering document or official statement for the issuance of the bonds. As a result, in preparing their offering documents, issuers must now weigh the applicability, significance and scope of ESG factors with respect to their financial condition, operations and overall investor mix. In this blog, we will discuss ESG disclosure practices, review the benefits and risks of including such disclosure and contrast general ESG considerations with specific green bond issuances.

Currently, neither the Securities and Exchange Commission nor the Municipal Securities Rulemaking Board ("MSRB") has weighed in with regulatory guidance as to ESG disclosure in the municipal marketplace. Some industry participants have argued for a uniform set of criteria or a checklist for ESG disclosure, as a means of promoting clarity and consistency. However, questions remain as to whether a "one size fits all" approach would be feasible for issuers and meaningful to investors, given the diversity of issuers and credits in the municipal space. Others have advocated for a principles-based approach, with general guidelines that issuers can apply and adapt to their particular facts and circumstances. The Government Finance Officers Association ("GFOA") has taken the lead role in this regard, releasing best practices for ESG disclosures.

Generally, the GFOA's ESG best practices focus on two main principles: (1) identifying and, if possible, quantifying the material ESG risks or factors affecting the issuer of the municipal bonds, specifically as they affect the issuer's operations and financial position, including its credit quality and ability to repay the bonds, as well as its infrastructure and ongoing projects (including projects to be funded with the bond proceeds) and (2) the policy actions to be taken by the issuer to address those risks/factors. In that regard, the environmental component of ESG is intended to address matters such as climate change and resiliency, energy efficiency and renewable energy. The social component focuses on diversity and inclusion, equity and social justice issues affecting the long-term sustainability of a community, such as income disparities, housing affordability, access to quality healthcare and public education and internet access and affordability. The governance component touches on the particular government's organizational structures, decision-making processes, budgetary practices, transparency, risk mitigation (cybersecurity), legal framework for the issuance of debt, financial reporting requirements and pension and OPEB liabilities. In that respect, it is likely that issuers are already addressing most of the topics under the governance component in their offering documents. Nevertheless, the current focus on ESG factors represents an opportunity for issuers to consider this information in a new light.

As a practical matter, the majority of projects financed with the proceeds of municipal bonds are likely to already fall within at least one of the three ESG categories. Nevertheless, ESG disclosure is intended to go beyond the specific projects, providing investors with a broader window into the issuer's overall operations and creditworthiness, with an emphasis on these factors.

It is worth noting that, under two key antifraud provisions of the federal securities laws, Section 17 (a) of the Securities Act of 1933 and Rule 10b-5 of the Securities Exchange Act of 1934, issuers must avoid making misstatements or omissions of material facts (with respect to ESG matters or otherwise) to investors in connection with the issuance and sale of municipal bonds to the public. Therefore, without a clear pricing differential or market advantage to offset this corresponding regulatory scrutiny, issuers may be understandably weary of including any new ESG disclosure in their offering documents. Additionally, to comply with MSRB Rule 15c2-12, underwriters involved in certain offerings of municipal bonds must confirm that the issuer will provide investors (through a filing with the MSRB) with annual updates to the financial information and operating data included in the offering document. Issuers should carefully consider whether any new ESG disclosure included in the offering document would be picked up by this annual reporting requirement.

Like ESG disclosure, issuances of bonds with particular labels such as "green," "climate," "social" or

"sustainable," where the proceeds are used to finance related projects, have increased in popularity during the past decade. Although the concepts have certain similarities, providing broad ESG disclosure about an issuer in an offering document does not necessarily transform the bond issue into green, climate, social or sustainable bonds. Likewise, providing specific project-related details in connection with an issuance of green, climate, social or sustainable bonds may capture some, but not necessarily all, of the ESG disclosure principles outlined above relative to the issuer. Stated differently, notwithstanding the potential for overlap, ESG disclosure focuses on the status of the issuer overall, whereas a labeled bond issue focuses on the use of the bond proceeds to finance a particular project or set of projects. Green bond disclosure guidance is currently under development by both the National Federation of Municipal Analysts and the GFOA in any event.

It appears that investor interest in ESG considerations will be with us for the foreseeable future. Issuers should work with their bond counsel, disclosure counsel, financial advisors and underwriters to develop a sensible approach to address this trend.

[1] For conduit issuers, attention should be paid to the issuer and the borrower when evaluating ESG factors.

Adler Pollock & Sheehan P.C.

October 29, 2021

SEC Charges School District and the District's Former Chief Financial Officer with Violations of Securities Laws in a 2018 Bond Offering.

On September 16, 2021, the Securities and Exchange Commission ("SEC") entered an order against a school district (Sweetwater Union High School District (the "District") in San Diego County, California) and charged the school district's former chief financial officer ("CFO") with misleading investors who purchased $28 million of the District's 2018 bonds (the "Bonds").

In its actions, the SEC noted that the District and its former CFO presented stale and misleading financial information in connection with the offering of the Bonds. Specifically, the District included misleading FY2018 budget projections in its offering document for the Bonds, which budget did not reflect salary increases approved prior to the start of FY2018. When the District's financial standing was being reviewed and then disclosed in the bond offering document, the District projected that its operations would result in a general fund balance of around $19.5 million when in reality, its operations resulted in a negative $7.2 million general fund balance; the District did not disclose that this projection was inconsistent with known actual expenses at that time. The former CFO's department generated reports that showed expenses trending higher than its budget projected, to which the SEC said the District "continued to ignore reports showing that its budget for the 2018 Fiscal Year was untenable." The District continued to use the stale budget projections in its reporting to the finance team1, the rating agency and eventually bond purchasers. Further, the former CFO attested to the accuracy of the information in the offering document when she signed the offering document, the bond purchase agreement and a certification to the underwriter.

The charges were brought under the Securities Act of 1933 Section 17(a)(2) and (3) for the District and 17(a)(3) for the former CFO; violations of these provisions do not require intentional wrongdoing on the part of the actor and can be established on the basis of negligence. Section 17(a)(2) and (3) provide, in relevant part, as follows:

> It shall be unlawful for any person in the offer of sale of any securities … directly or indirectly – …
>
> (2) to obtain money or property by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading; or
>
> (3) to engage in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon the purchaser.

"A statement or omission is material if there is a substantial likelihood that a reasonable investor would consider it important in making an investment decision."2

The SEC order against the District found that the District violated Section 17(a)(2) and (3) by "making misleading statements and omissions to investors, as well as to the bonds' credit rating agency and other municipal industry professionals on the transaction." The District was ordered to cease and desist violating Section 17(a)(2) and (3), implement various written policies and procedures, conduct staff training, retain an independent consultant to review the policies and procedures, implement recommendations of the independent consultant, disclose this settlement in future bond offerings, and provide certifications of compliance to the Staff of the SEC regarding these settlement conditions.

The SEC charged the former CFO with violating section 17(a)(3). The former CFO has agreed to settle with the SEC, including being enjoined from participating in any future municipal securities offerings and paying a $28,000 penalty. The settlement is pending court approval.

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1 The finance team consisted of the underwriter and its counsel, bond counsel, disclosure counsel and the District's municipal advisor.
2 Securities Act of 1933 Release No. 10981, September 16, 2021, citing Basic Inc. v. Levinson, 485 U.S. 224, 231-32 (1988).

Dorsey & Whitney LLP

by Jennifer Block, John Danos, David Grossklaus, Cristina Kuhn, James Smith

October 27, 2021

GFOA: Meaningful Disclosure Encouraged in ESG by State and Local Governments

GFOA's Executive Board approved several new best practices on the Social and Governance factors of ESG and Disclosure as well as a comprehensive best practice on voluntary disclosure. Similar to action taken in 2019 to establish the Disclosure Industry Workgroup, the GFOA has taken a leadership role in our market to develop a pragmatic approach to encouraging meaningful disclosure in the area of ESG by state and local governments.

Publication date: October 2021

DOWNLOAD FULL RELEASE

GFOA Best Practices in ESG Disclosure: Social

Social

It is important for issuers to consider the social factors that are challenging their community and decide if any have a connection to repayment of their bonds or could negatively impact operations or financial position over the term of its debt.

DOWNLOAD BEST PRACTICE

GFOA Best Practices in ESG Disclosure: Environmental

Environmental

The increase in the number of extreme weather events in recent years has raised public awareness about climate change. Investors and rating analysts are not just looking to see if risks are present, but also want information regarding what plans a government has to address these risks.

DOWNLOAD BEST PRACTICE

GFOA Best Practices in ESG Disclosure: Governance

Governance

Governance factors have always been a part of government management, operations, and finances. Governance includes governmental decision-making, policies, legal requirements, organizational structure, and financial and budget management practices.

DOWNLOAD BEST PRACTICE

MSRB Requests Comment on Draft Compliance Resources for Supervisors: Cadwalader

The MSRB requested comment on draft compliance resources to assist regulated entities in their supervision over new issue pricing of municipal securities. The MSRB stated that “the goal of the compliance resources is to enhance understanding regarding the existing regulatory standards applicable to regulated entities’ supervision of conduct when pricing a new issuance of municipal securities.”

One proposed compliance resource would focus on underwriting activity under MSRB Rule G-17 (“Conduct of Municipal Securities and Municipal Advisory Activities”) and supervisory obligations

under MSRB Rule G-27 (“Supervision”). The second resource would focus on duty of care obligations under MSRB Rule G-42 (“Duties of Non-Solicitor Municipal Advisors”) and non-solicitor municipal advisors’ duties under MSRB Rule G-44 (“Supervisory and Compliance Obligations of Municipal Advisors”).

Both proposed resources would summarize the relevant rule requirements, provide responses to FAQs and offer “Questions for Consideration” to help entities design their compliance procedures.

The MSRB specifically requested comment on the following issues, among others:

- the relevance of the questions posed and the usefulness of the responses given in the FAQs;
- the format of the resources;
- the language of the draft compliance resources in conveying the “flexibility” afforded to entities in tailoring their supervisory systems; and
- whether the MSRB should amend the abovementioned rules or adopt formal interpretive guidance expressly to define new issue pricing obligations.

Comments on the compliance resources must be submitted by January 4, 2022.

Cadwalader Wickersham & Taft LLP

October 6 2021

Banks Press Ahead with Term SOFR Preparation; Credit Sensitive Rates Under Scrutiny: McGuireWoods

Where we left off: In our Mid-Year Check-In blogpost, we noted that progress in the development and readiness of some credit sensitive interest rate indices (e.g., Bloomberg’s BSBY, IBA’s Bank Yield Index and American Financial Exchange’s AMERIBOR) seemed to spark some urgency in the development of SOFR’s forward-looking term rate in Q2, including the ARRC’s selection of CME Group as administrator for Term SOFR, and the CFTC’s SOFR First Initiative to encourage primary market swaps dealers to quote USD swaps at SOFR. Those efforts culminated in the ARRC’s formal recommendation of Term SOFR for use in the bank loan market on July 29, 2021.

The LSTA followed up by releasing a Concept Credit Agreement for Day-One Term SOFR, and now many bank clients have developed day-one Term SOFR language in their own form documents in anticipation of issuing new loans at Term SOFR in Q4.

SOFR Deals Debuting. Both Daily Simple SOFR and Term SOFR have started to see actual use cases in the market in Q3:

- Some term sheets in the market include provisions to toggle over to day one Daily Simple SOFR or Term SOFR if they close after a certain date (e.g., December 31, 2021 or in some cases earlier).
- Two of Ford Motor Company’s credit facilities led by JP Morgan Chase Bank, N.A. transitioned to daily simple SOFR on September 29,[1] providing the market with a look at how that variety of SOFR operationalizes in real time.
- Several sources (Covenant Review; Bloomberg; LSTA) reported seeing the first Term SOFR term sheet, a loan for the acquisition of Sanderson Farm.
- Bloomberg and the LSTA have noted a JPMorgan Chase Bank, N.A. led deal for Walker & Dunlop with a TLB priced at SOFR.

One issue to watch in the development of day one SOFR deals: whether the rate is constructed as a three part calculation (SOFR + spread adjustment (used to approximate LIBOR) + applicable margin) or a two part calculation (SOFR + applicable margin, loading any implied spread to LIBOR into the applicable margin). The spread adjustments fixed by the ARRC at the end of Q1 used the average delta between SORF and LIBOR over the prior 5 years – the LIBOR spread over SOFR is now much lower in our current environment of historically low interest rates. As a result, lenders have been watching to see whether the spread adjustment becomes a hotly negotiated point in a three part construct, or subsumed into the negotiation of the applicable margin in a two part construct. Banks may need to operationalize a dual tracking system if both approaches remain in the market.

Do you have a license for that? LIBOR became so ubiquitous in the bank loan market that its status as a licensed product faded into the background, but LIBOR is a rate administered and licensed for use by the ICE Benchmark Administration (IBA), and financial institutions using LIBOR are required to enter into a license agreement with the IBA for its use. CME Group is licensing its publication of Term SOFR on largely the same basis, and market participants are now familiarizing themselves with CME Group's license categories and use restrictions in anticipation of booking loans at Term SOFR in Q4. A summary of CME Group's license tiers can be found at cmegroup.com. At a high level, it seems clear that an administrative agent running a syndicated lending transaction needs a license, as does each member of the syndicate using the published Term SOFR rates to make its own interest calculations; the "end-user" borrower would not, unless the borrower is independently using the CME Group's published rates to run its own models and analytics. The takeaway: if you plan to use Term SOFR as an agent or to run your own models, you'll need one; if you're unsure, check in with CME Group.

What about those Credit Sensitive Rates? The rapid progress of Term SOFR over the summer hasn't stopped loan market participants from preparing to offer credit sensitive rates as an alternative, and in both their systems and loan document forms, despite the comments of SEC Chair Gary Gensler at the June 2021 FSOC Meeting.

The official sector, however, continues to preach caution on the robustness of credit sensitive alternatives:

- The International Organization of Securities Commissions ("IOSCO"), which previously established Principles on Financial Benchmarks for evaluating LIBOR alternatives, on September 8 issued a statement specifically calling for greater attention to its Principle 6 (relative size of the underlying market in relation to the volume of trading) and Principle 7 (data sufficiency in a benchmark's design to accurately and reliably represent the underlying market) in evaluating credit sensitive rates.
- SEC Chair Gensler led off the Fifth SOFR Symposium on September 20 by restating and amplifying his FSOC meeting concerns about the thin (or in times of economic stress, likely non-existent) market in unsecured term bank-to-bank lending underlying BSBY and other credit sensitive rates.
- In comments at a Structured Finance Association conference in Las Vegas on October 5, Vice-Chair of the Federal Reserve Randal Quarles again focused on the need for banks to move quickly away from new LIBOR loans by the end of 2021, and emphasized that regulators will be paying close attention.

Many banks have established October or November internal deadlines for "no new LIBOR" to provide cushion for the very clear regulatory December 31 cutoff, so we expect to see rapid progress in market adoption of, and adaptation to, both SOFR-based and credit sensitive rates throughout Q4. We'll be watching and advising on how it evolves for our financial institution clients.

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[1] https://www.sec.gov/Archives/edgar/data/37996/000003799621000079/exhibit101toseptember29202.htm; https://www.sec.gov/Archives/edgar/data/37996/000003799621000079/exhibit102tosep

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By Donald A. Ensing & Susan Rodriguez on October 12, 2021

LIBOR Transition Blog

McGuireWoods

GFOA Priorities Face Uncertainty as Infrastructure Vote Delayed.

After a tense week of negotiations on Capitol Hill that included a rare visit from the President and visible interparty disagreement, Speaker Nancy Pelosi was forced to delay the highly anticipated vote on the bi-partisan Infrastructure Investment & Jobs Act (IIJA). Lawmakers had originally been told the vote would be held no later than September 27, but fears over missing that deadline were realized when the vote was pushed to the September 30. Once it became clear that opposition to the bill was steadfast among progressive Democrats, Speaker Pelosi had no choice but to punt the vote further into the calendar, which places a cloud of uncertainty over the GFOA muni bond provisions that currently sit in the House version of a budget reconciliation bill. **GFOA member outreach on issues like restoring advance refunding and increasing the small borrower/bank qualified limit will be critical in the coming weeks.**

Driving much of the disarray is a sharp difference between moderate and progressive Democrats who disagree on the topline spending figures of President Biden's legislative priorities. Earlier in the year, progressive Democrats in the House made clear that support for the Senate-passed IIJA was contingent on a commitment to the budget reconciliation bill that satisfied their legislative goals. But moderate members of the Senate, chiefly Senators Joe Manchin (D-WV) and Kyrsten Sinema (D-AZ), have balked at the lofty $3.5 trillion price tag of the budget bill, leading to the twenty-four-hour negotiation crunch that played out during the final days of September.

As a result, on October 4, Speaker Pelosi set a new deadline of October 31 to vote on the infrastructure bill. Congressional Democrats will have the rest of the month to bridge the sizeable gaps both within their party and across the aisle with the hope of moving forward on both packages.

GFOA's Federal Liaison Center (FLC) created an overview page on the muni bond priorities to help members as they reach out to their respective congressional delegation. Click here for a brief summary and additional resources on the priorities.

GFOA's FLC will continue to monitor this legislative activity.

SEC Approves Changes to MSRB Customer Disclosure Rules.

Per BDA advocacy – the SEC approves changes to MSRB customer disclosure rules.

For more information please click here.

BOND DEALERS OF AMERICA

OCTOBER 6, 2021

UBS's Botched Muni Statements Cost Clients Millions, Suit Says.

- **Bank error allegedly inflated muni investors' taxable income**
- **Suit says UBS won't issue corrected statements to all clients**

UBS Financial Services cost clients "at least tens of millions of dollars" by incorrectly reporting tax information to holders of taxable municipal bonds, a lawsuit alleges.

The bank, which oversees more than $90 billion of municipal bonds, didn't report amortizable bond premium on forms clients use to prepare tax returns, resulting in "substantial" overstatement of taxable income and overpayment of taxes, according to a proposed class action suit filed on Tuesday in New Jersey federal court.

U.S. Treasury rules allow investors who buy a taxable bond for more than its face value to amortize the premium over the remaining life of the bond to reduce taxable income. But UBS reported only the gross amount of interest on clients' federal 1099 forms, the suit alleges.

UBS spokeswoman Alison Keunen said the bank disputes the allegations in the suit and intends to vigorously defend itself. The Swiss bank has more than 1 million clients.

Richard M. Goodman brought the suit on behalf of customers who bought taxable municipal bonds in accounts maintained by UBS on or after January 1, 2014. Goodman said in the suit that his own UBS financial adviser, Brian Edgar, notified the bank's municipal bond and tax departments in 2016 that it was incorrectly reporting the amortizable bond premium.

Over-Reported Income

Edgar was able to get UBS to issue amended 1099 forms to his clients. Goodman said he received corrected tax documents, showing the bank overstated his taxable income from 2015 through 2018 by more than $100,000. Other clients of Edgar's had their taxable income over-reported by tens or hundreds of thousands of dollars, the suit claims.

According to Goodman, UBS declined to address this issue for all of its clients. He said he was told UBS would issue corrected statements if a client or their financial adviser raised the issue.

"Defendant purposely continued its incorrect and harmful practices, and failed to promptly and fully correct its prior erroneous tax information reporting upon learning of the error," Goodman said.

In addition to federal income tax overpayments, hundreds of UBS clients nationwide were harmed because they received smaller tax refunds than they were entitled to and incurred unnecessary expenses for tax preparers and advice, the complaint said. The lawsuit alleges negligence and breach of contract, among other claims.

'Firm-Wide Deficiencies'

UBS has previously drawn regulatory action for inaccurately reporting the tax status of municipal bond interest payments. It was fined $750,000 in 2015 and $2 million in 2019 by the Financial

Industry Regulatory Authority for misstating that interest paid to thousands of customers on their municipal bond holdings was tax-exempt. UBS was required to pay restitution to customers for any increased tax liabilities.

Interest payments from bonds issued by state, city and local governments are generally free from federal income taxes and income taxes in the state where the bonds was issued, with some exceptions. However, municipalities have issued taxable bonds for purposes like financing sports facilities, funding industrial development, improving public pension funding levels or refunding previously refinanced municipal bonds. Universities issue taxable munis for projects or purposes that don't qualify for tax-exempt financing.

More than $620 billion of taxable muni bonds without corporate security identifiers are outstanding, accounting for 16% of the $4 trillion market, according to data compiled by Bloomberg.

The case is Richard Goodman, Individually And As Trustee of the Richard M. Goodman Revocable Living Trust, And on Behalf Of All Others Similarly Situated vs. UBS Financial Services Inc., 21-c--18123, U.S. District Court, District of New Jersey

Bloomberg Markets

By Martin Z Braun

October 7, 2021, 7:35 AM PDT

— *With assistance by Natalia Lenkiewicz*

[UBS Sued Over Muni-Bond Snafu that Cost Clients.]

UBS Financial Services misreported interest paid on taxable munis, resulting in higher tax bills for clients, according to a lawsuit.

UBS Financial Services Inc. is facing a new lawsuit that claims the firm's problems with tax reporting on municipal bonds overstated clients' taxable income, costing clients higher tax bills and creating potential damages.

Beginning with the 2014 tax year, UBS "incorrectly reported certain tax information to its clients relating to interest paid on taxable municipal bonds," according to the complaint, which was filed Tuesday in U.S. district court in New Jersey.

The plaintiff, Richard Goodman, resides in Michigan, and UBS allegedly admitted it had overstated his taxable income by $100,000 for 2015 to 2018, according to the complaint, which is seeking class action status.

Overstating a client's income results in "substantial" overpayments of federal income taxes, according to the complaint.

Goodman's financial adviser at UBS in Michigan was Brian Edgar, according to the complaint. He left UBS last year and now works at Wells Fargo Advisors in Florida, according to his BrokerCheck report.

Improper reporting of interest paid on taxable municipal bonds is violation of Treasury regulations

and UBS' own policies, according to the complaint.

UBS "failed to report amortizable bond premium for taxable municipal bonds as required by applicable Treasury regulations," according to the complaint. The firm's "incorrect tax information reporting to clients had the effect of substantially overstating the clients' taxable income costing money" to Goodman and other clients.

According to the complaint, the overall size of the municipal bond market is in the range of $3.8 trillion to $4 trillion.

"UBS disputes the allegations in the complaint and intends to vigorously defend against the lawsuit," said a UBS spokesperson on Friday morning.

Edgar did not return a call at Wells Fargo Advisors to comment.

The complaint sites two Finra actions against UBS involving municipal bonds, from 2015 and 2019. Most recently, the Financial Industry Regulatory Authority Inc. censured and fined UBS Financial Services $2 million for "repeated failures" in addressing municipal short positions in a timely way and for inaccurately representing the tax status of thousands of interest payments to customers.

Interest payments from municipal bonds are generally subject to federal income taxes if the bond proceeds are used for a purpose that substantially benefits private interests, and such bonds are called taxable municipal bonds, according to the complaint.

The interest payments from such bonds are often free from state and local income taxes in the state or locality where the bond was issued, with some exceptions.

investmentnews.com

By Bruce Kelly Bruce Kelly

October 8, 2021

UBS Faces Lawsuit Over Alleged Muni Misreporting.

UBS allegedly misreported tax information on taxable municipal bonds, costing its clients millions of dollars, according to news reports.

The company allegedly failed to report amortizable bond premiums on forms used by clients to prepare their taxes, which led to "substantial" overstatement of taxable income and subsequently cost clients "at least tens of millions of dollars," Bloomberg writes, citing a proposed class action lawsuit filed by Richard Goodman on behalf of himself and other customers who bought taxable municipal bonds in accounts maintained by UBS on or after Jan. 1, 2014.

The suit claims that Goodman's own financial advisor, Brian Edgar, told the firm's municipal bond and tax departments in 2016 about the errors in reporting the amortizable bond premium, according to the news service.

Edgard got UBS to amend 1099 forms for his clients, at which point Goodman learned that UBS had overstated his taxable income from 2015 through 2018 by more than $100,000, Bloomberg writes. The suit claims that Edgar's other clients' taxable income was overstated by tens or hundreds of

thousands of dollars, according to the news service.

Moreover, Goodman claims in the suit that he learned that UBS would not amend the errors automatically but would only do so if a client or their advisor brought it up, Bloomberg writes.

“Defendant purposely continued its incorrect and harmful practices, and failed to promptly and fully correct its prior erroneous tax information reporting upon learning of the error,” Goodman said, according to the news service.

UBS spokeswoman Alison Keunen tells Bloomberg that the firm disputes the allegations and plans to vigorously defend itself.

Earlier this week, Merrlll Lynch agreed to pay $1.5 million to settle claims brought by the Financial Industry Regulatory Authority alleging violations related to short sales in municipal securities, as reported.

financialadvisoriq.com

October 8, 2021

FINRA Proposes Fee for New Municipal Advisor Principal Exam.

FINRA proposed establishing new fees for the new Municipal Advisor Principal Examination (a/k/a the Series 54 exam). Under the proposed amendment to Section 4(c) of Schedule A to its By-Laws, FINRA would establish a $115 fee to account for examination administration and delivery expenses.

Comments on the proposal must be submitted within 21 days of its publication in the Federal Register.

Cadwalader Wickersham & Taft LLP

September 27 2021

SLFRF Recipients: Treasury Extends Reporting Deadline

The U.S. Department of Treasury has extended the reporting deadline for the Project & Expenditures Report for all recipients of the Coronavirus State and Local Fiscal Recovery Fund (SLFRF).

- **States, Metropolitan Cities, Counties, Territories, and Tribal Governments will now report on January 31, 2022**, instead of October 31, 2021.
- The first reporting deadline for **Non-Entitlement Units (NEUs) will be April 30, 2022**, instead of October 31, 2021.
- States have been sent a draft letter regarding the change by the Treasury which can be used to notify their NEUs.

Additional updates to existing guidance as well as a user guide to assist recipients with the reporting portal will be released at a later date.

GFOA's Federal Liaison Center will continue monitoring for updates.

ESG Issues on the 'Mind' of the Muni Market's Regulator.

- **MSRB's Kim says regulator is looking at rise of ESG in munis**
- **New strategic plan includes promoting diversity in industry**

The head of the $4 trillion municipal securities market's regulator said the explosion of environmental and socially minded investing is an area it's watching closely.

Mark Kim, chief executive officer of the Municipal Securities Rulemaking Board, said in an interview that the board is focused on the quickly growing environmental, social, and governance sector of the market.

And he said it's possible that the U.S. Securities and Exchange Commission could start looking at it as well after its chairman, Gary Gensler, said this month that he's asked his staff to look into ways to bring transparency to asset classes like municipals.

"ESG is going to be one of the issues that will be on our mind and will be on the mind of the SEC as well when it comes to the municipal securities market," said Kim, who took his post last year. He said the MSRB is interested in the issue from the point of view of disclosure.

ESG was one of the areas mentioned in the MSRB's strategic plan it's releasing Monday, which will guide its activity for fiscal 2022 through 2025. The plan outlines goals, such as modernizing its rulebook and using data to strengthen market fairness.

ESG investing has grown in popularity in the muni market as it has in other asset classes. Sales of green muni bonds remain strong, with more than $10 billion sold in 2021, and some investment firms have debuted funds focused on sustainable investments. But municipal issuers still aren't disclosing enough information around risks, such as those related to the environment, according to a July report by Principles for Responsible Investment, a United Nations-backed group that promotes sustainable investing.

The MSRB's strategic plan says the regulator will "coordinate with regulatory and industry efforts, promote dialog and use MSRB data to inform the market's understanding of environmental, social and governance (ESG) factors and emerging issues." Kim said the MSRB plans to issue a request for information before the end of the year to get feedback from members of the industry on the topic.

Diversity Goal

The MSRB's strategic plan also says the regulator has a commitment to "diversity, equity and inclusion" and mentioned the importance of seeking diverse perspectives when coming up with its rules.

Kim said that starts with the MSRB's governance, and said he's proud that women make up two-thirds of its new board starting in October. It's partnering with the Financial Industry Regulatory Authority on an initiative to better understand the challenges facing minority- and women-owned businesses in the industry and if there are any "undue" burdens that MSRB rules place on them, he said.

“This is a really important question — it’s one that we’re going to engage on directly with market participants, and we’re also partnering with our fellow regulators to address this issue more systemically across the entire financial services industry,” Kim said.

Bloomberg Markets

By Amanda Albright

September 20, 2021, 9:00 AM MDT

GASB Fact Sheet on the Proposed Note Disclosure Concepts Statement.

View the GASB Fact Sheet.

[09/23/21]

US Bond Lobbies Warn SEC of Severe Disruption Under Rule Change.

Lobbying groups warn that activity in the world’s largest bond market could stop at the end of this month without last-minute exemption from the vague US 50-year-old rule that previously aimed only at equities. doing.

Bond industry groups have told regulators that the revised rules will have a “significant and detrimental effect” on the government and corporate bond markets, calling for more time for explicit grace or compliance. The amendment was first proposed last year, but market participants assumed that until the last few months, the rules would only relate to the stock market.

“We believe that the application of such rules is widespread and unnecessary,” writes the American fixed income dealers, securities industry and financial markets associations.

The SEC’s 1971 statute, known as “Rule 15c2-11,” “Publishing or submitting” Of the price for buying and selling securities away from the exchange. Market participants primarily believe that this is an attempt to protect retail investors from predatory plans and fraudulent activity in Penny shares.

This rule requires broker-dealers such as JPMorgan Chase and Citi to review a wide range of information about publishers, including quarterly and annual reports. Last year, the SEC, led by Jay Clayton, fine-tuned the rules for the first time in almost 30 years and included requirements for disclosure of information.

“Improvements to Rule 15c2-11, which focuses on these individual investors, have been delayed for a long time,” said Clayton at the time, and technological advances allow investors to be more up-t--date before trading. I added that I can do it.

The law has not explicitly excluded bonds, but in reality it has never been applied to bonds for a lifetime of 50 years. This has long been suitable for markets where many corporate issuers are not listed on the stock market and do not regularly produce regular earnings reports. It is unclear what disclosure will be required for government bonds, such as government bonds issued by the US Treasury.

However, BDA Vice President of Policy and Research Michael Decker said the SEC, led by new chief Gary Gensler, will also affect government and corporate bonds under the amendments outlined last year. He said he confirmed. Only municipal bonds have an explicit exemption.

“It’s been a few days here and little work has been done. It’s pretty clear to me that the SEC didn’t really think about this,” Decker said.

The SEC declined to comment.

Bankers, trading platforms and investors are facing stringent compliance requirements ahead of unexpected end-of-month deadlines, and growing awareness of new requirements is disrupting bond markets.

Without guidance and amendments from the SEC, broker-dealers will withdraw for fear of attracting enforcement action from securities regulators, and some bond market transactions will stop when the rules come into force at the end of this month. I am concerned about that.

The SEC’s move has come a time of increased regulatory scrutiny of fixed income transactions, and Gensler said this month it intends to bring greater efficiency and transparency to the market.

Broker-dealers are struggling to understand how to collect, verify, and publish information about companies that trade bonds. They also question what counts as a bond quote is published or submitted, a term that is not defined in the rules.

Bond trading is increasingly shifting to electronic venue trading, with prices being streamed to the screen. To avoid market disclosure, some market participants may return the transaction to the phone until clearer guidance is available.

“The risk is that if a broker-dealer feels out of compliance based on the interpretation of an internal team, he may be forced to stop quoting certain bonds to avoid non-compliance,” Kevin said. • McPartland states. Head of Research, Market Structure and Technology at Greenwich Associates.

California News Times

SEC Sues Muni Advisers in First Case Over Bank Fee Splitting.

- **Advisers failed to disclose deal to charter school clients**
- **Regulator charged Choice Advisors and two principals**

A firm that advises charter schools on bond issues was sued by the Securities and Exchange Commission for allegedly making an undisclosed fee-splitting agreement with an underwriter, in what the agency said was its first case of enforcing code-of-conduct rules ushered in after the 2008 financial crisis.

Choice Advisors LLC and its two principals, Matthias O’Meara and Paula Permenter, failed to disclose to their clients the conflicts of interest associated with “the illicit arrangement or their relationship” with an investment bank where they previously worked, the SEC said in a statement. Fee-splitting arrangements are prohibited in any bond deal where the municipal adviser provides advice to clients of the underwriter.

O’Meara and Permenter started the Texas- and Colorado-based Choice in 2018 to advise clients on

bond sales. The two were employed by BB&T Securities LLC until that year, according to financial registration records. BB&T, which merged with SunTrust Bank in 2019 to form Truist Financial, wasn't charged by the SEC.

The SEC also alleged that O'Meara, while still employed at the investment bank, simultaneously served as a banker and as an adviser for two clients, a conflict that is at odds with an adviser's fiduciary duty. O'Meara allegedly took steps to increase the overall fees paid by the clients to enrich himself and Choice, costing one school about $40,000 in additional fees, according to the SEC.

Conflicting Interests

"Schools and other municipal entities should be able to trust that municipal advisers are serving their clients' interests and not their own," LeeAnn Gaunt, chief of the SEC Enforcement Division's Public Finance Abuse unit, said in a statement.

Such financial advisory firms act on behalf of governments and nonprofits that are raising money in the bond market, seeking to ensure the clients get the best possible borrowing costs. That can put them in opposition to underwriters, which have an incentive to set the yields on bonds high enough so that they can easily be sold. The advisory business was subject to regulations under the Dodd-Frank law after states and governments were hammered by losses on risky bond deals that went haywire during the credit crash.

The SEC said that Choice and its principals also failed to register with the agency or Municipal Securities Rulemaking Board, as required under the law.

Permenter agreed to settle with the SEC without admitting or denying the allegations. She was censured and ordered to pay a $26,000 penalty.

O'Meara and Choice, who didn't settle, were charged with violating the municipal adviser fiduciary duty, deceptive practices, fair dealing and registration provisions of the federal securities law. Paul Maco, an attorney at Bracewell who is representing O'Meara and Choice, didn't immediately respond to a request for comment. Kyle Tarrance, a spokesperson for Truist, declined to comment.

Bloomberg Markets

By Martin Z Braun

September 23, 2021, 1:14 PM MDT Updated on September 23, 2021, 2:10 PM MDT

SEC Files Muni Bond Action Centered on Flippers.

Municipal bonds are an important area in which few cases are typically filed. Frequently, when a case is filed it focuses on the financial information included in an offering which is at times not updated as required. Another key area, however, involves "flippers," that is, those who improperly obtain bonds in an offering not for an investment but to sell to others. Offering procedures for municipal bonds typically prioritize investors over flippers. Yet there are increasing numbers of cases where the offering procedures are thwarted. This week the Commission brought another case based on flippers.

In the Matter of Kenneth G. Bredrich, Adm. Proc. File No. 3-20569 (September 17, 2021) is an action

which named as a respondent the registered representative. He was employed at Major Broker. The internal procedures of Major Broker required that municipal bond sales be prioritized to allocate bonds per a standard methodology that prioritized customers and dealers over flipper absent different instructions from issuers. Over a four-year period beginning in 2014, however, the firm in a number of instances failed to follow the procedures. Indeed, at times Major Broker used the flippers to circumvent issuer priorities. As a result, the Order alleges violations of Exchange Act Section 15B (c)(1). To resolve the proceedings, Respondent consented to the entry of a cease-and-desist order based on the Section cited in the Order and to a censure. In addition, Respondent shall not act in the securities business or negotiate the purchase and sale of municipal bonds for a period of six months. He will also pay a penalty of $30,000. S*ee also In the Matter of Jaime I. Durando,* Adm. Proc. File No. 93044 (September 17, 2021)(Respondent is also employed by Major Broker and engaged in essentially the same conduct as above; resolved with a cease-and-order based on the same Section and the payment of a $25,000 civil penalty).

September 23 2021

SEC Actions

MSRB Outlines Strategic Plan for Next Four Years: Cadwalader

The MSRB released its fiscal year 2022-2025 strategic plan for improving and protecting the municipal securities market.

The MSRB's goals include:

- updating the MSRB's rulebook in a "prudent and practical" manner to encourage capital formation and support a fair and efficient market;
- leveraging technology to improve the Electronic Municipal Market Access (EMMA®) system;
- producing useful, high quality market data; and
- prioritizing the MSRB's "commitment to social responsibility, diversity, equity and inclusion."

The MSRB stated that its new fiscal year will begin on October 1, 2021. The Board intends to publish an annual budget with further information on "near-term organizational priorities" in line with its strategic plan.

Cadwalader Wickersham & Taft LLP

September 20 2021

MSRB Strategic Plan Advances Mission to Protect and Strengthen the Municipal Securities Market, Giving America the Confidence to Invest in Its Communities.

Washington, DC – The Municipal Securities Rulemaking Board (MSRB) has published its new strategic plan for the next four years. The strategic plan advances the MSRB's mission to protect and strengthen the municipal bond market, enabling access to capital, economic growth, and societal progress in tens of thousands of communities across the country.

“Our vision is to give America the confidence to invest in its communities,” said Mark Kim, CEO of the MSRB. “As we eventually emerge from the pandemic, communities will drive economic growth and recovery by investing in public infrastructure, the majority of which will be financed through the $4 trillion municipal securities market that we are entrusted to regulate.”

Under the leadership of the Board of Directors, the MSRB developed the strategic plan in close collaboration with stakeholders. The plan lays out four strategic goals for Fiscal Years 2022-2025:

Market Regulation: Modernize the rule book through a prudent and practical approach that promotes a fair and efficient market and facilitates capital formation

Market Transparency: Leverage investments in the cloud and in our people to enhance the value of EMMA ® as a platform that benefits all market participants and the public

Market Data: Provide high quality market data that enable comprehensive analysis and insight of the municipal securities market

Public Trust: Uphold the public interest and the integrity of the municipal market across all of the MSRB’s strategic goals and initiatives, including a commitment to social responsibility, diversity, equity and inclusion

“We’ve established three guiding principles to define how we will go about advancing this multi-year strategic plan,” Kim said. “First, we will continue to adhere to our Congressional mandate. Second, we will engage with our diverse stakeholders by facilitating dialogue and serving as a forum for discussion of evolving market topics. Third, we will ensure accountability to the public through greater transparency and inclusivity as we make progress on and advance these strategic goals.”

The MSRB begins its new fiscal year on October 1, 2021 and will publish the annual budget with additional detail on near-term organizational priorities aligned with the long-term plan.

Date: September 20, 2021

Contact: Leah Szarek, Chief External Relations Officer
202-838-1300
lszarek@msrb.org

SEC, MSRB and FINRA to Offer Compliance Outreach Program: Cadwalader

The SEC, the MSRB and FINRA will be offering a 2021 Compliance Outreach Program for municipal advisors. The program is scheduled for October 7, 2021. The program is intended to facilitate a dialogue between municipal advisers, municipal market participants and the agencies regarding regulatory issues. The program will include topics on (i) conflicts of interest disclosures, (ii) new issue pricing, (iii) examination preparation and (iv) agency observations and enforcement actions. In addition, there will be a presentation regarding use of the EDGAR system.

FINRA is administering registration for the program, which is free and open to the public

September 20 2021

Cadwalader Wickersham & Taft LLP

Intriguing FINRA Enforcement Action In the Bond Market: More to Come? - Arent Fox

In June, FINRA reminded broker-dealers of their best execution obligations which are derived from common law agency principles and fiduciary obligations. The best execution obligation is incorporated in applicable MSRB rules and, through judicial and Securities and Exchange Commission (SEC) decisions, in the anti-fraud provisions of the Federal securities laws.

[For Our Complete Archive of LIBOR Analysis Click Here]

In 2021, the Financial Industry Regulatory Authority (FINRA) enforced the "best judgment" requirement for publishing prices related to municipal securities. In the same action, FINRA found that the broker-dealer violated MSRB rules related to fair dealing and supervision.

In addition, in June, FINRA reminded broker-dealers of their best execution obligations which are derived from common law agency principles and fiduciary obligations. The best execution obligation is incorporated in applicable MSRB rules and, through judicial and Securities and Exchange Commission (SEC) decisions, in the anti-fraud provisions of the Federal securities laws.

These actions may signal that FINRA is preparing to bring additional enforcement actions relating to the best judgment and best execution rules. [1]

In fact, on September 14, 2021, the SEC Chairman testified before the Senate Banking, Housing, and Urban Affairs Committee, where he stated (the "Senate Banking Gensler Testimony"):

> The U.S. capital markets represents 38 percent of the globe's capital markets. [In addition to examining the Treasury market], I've asked staff for recommendations on how we can bring greater efficiency and transparency to the non-Treasury fixed income markets – corporate bonds, a $11 trillion market; municipal bonds, a $4 trillion market; and [mortgage and] asset-backed securities (which back mortgages, automobiles, and credit cards), a $13 trillion market.This market is so critical to issuers. It is nearly 2.5 times larger than the commercial bank lending of about $10.5 trillion in our economy.

Relevant Governmental Regulators

FINRA

FINRA is a self-regulatory organization working under the supervision of the SEC. As the largest dispute resolution forum in the securities industry, FINRA resolves securities-related disputes. It also educates investors, and enacts and enforces rules governing the ethical activities of all registered brokers and registered broker-dealers in the United States.

As a self-regulatory organization, the FINRA Board is comprised of both regulated industry representatives and public representatives.

According to FINRA Rule 2010, registered broker-dealers and registered brokers are required to:

> [o]bserve high standards of commercial honor and just and equitable principles of trade

FINRA primarily issues rules with respect to the corporate securities market. This market's size was $10.6 trillion, with new issuance volume of $2.3 trillion in 2020.

MSRB

Like FINRA, the MSRB is a self-regulatory organization under the oversight of the SEC. In forming the MSRB, the Senate Committee on Banking, Housing, and Urban Affairs expressed hope in 1977, " that a self-regulatory body like the MSRB would develop prophylactic rules for the industry, which would preemptively deter unethical and fraudulent practices". [2]

Its mission, as set forth on the MSRB's web page, is to protect investors, state and local governmental issuers, other municipal-related entities (including conduit borrowers) and the public interest.

The MSRB was created in the 1970's, when New York City was on the brink of default, to prevent fraudulent and manipulative acts and practices of some broker-dealers. Over the ensuing decades, there were other crises impacting the municipal industry including (i) the $2.3 billion default of bonds issued by the Washington Public Power System Supply ("WPPSS"; commonly referred to in the bond industry as 'Whoops') in 1983 caused by increased costs and delays in nuclear power plant construction, and related inadequate disclosure to investors, (ii) the bankruptcy of Orange County, California in 1994 precipitated by its overreliance on risky investments, including derivatives, which were also not adequately disclosed [3] and (iii) the bankruptcy of Jefferson County, Alabama due to the increased expense of rebuilding its sewer system necessitated by U.S. Environmental Protection Administration violations, and its overreliance on costly interest rate swaps for the variable rate bonds it issued to finance the sewer system improvements.

In 2020, the municipal securities market's size was $3.9 trillion, with new issuance volume of $494 billion. According to Moody's Investors Service, Inc., the default rate average from 2010-2019 was 0.10% for municipal securities compared to a default rate of 2.25% for corporate securities.

Rulemaking

Historically, MSRB Rules were "principles-based" with specific guidance given where appropriate. MSRB is in the process of updating its rules and related guidance.

MSRB Rules generally fall into the following categories:

professional qualification

- fair practice rules to protect investors, municipal entities, conduit borrowers and the general public – *best execution, suitability, material investor and conflicts of interests disclosures; transparent pricing; pay-to-play; municipal advisor obligations*
- uniform practice – *standard confirmation, underwriting and settlement procedures*
- market transparency – *primary offerings; real-time reporting of trade prices*
- regulated entity administration – c*ompliance; proper recordkeeping; supervision of professionals*

According to the MSRB, these rules require regulated entities to:

> observe the highest professional standards in their activities and relationships with customers and municipal entities, and go significantly beyond the general anti-fraud principles of the federal securities laws

Lack of Enforcement Powers

Notwithstanding the foregoing rulemaking authority, responsibility for inspection and enforcement of MSRB Rules rests with the following Federal government and self-regulatory bodies:

- FINRA
  securities firms
- SEC
  municipal advisors, and all securities firms and banks
- Federal Deposit Insurance Corporation (FDIC)
- Board of Governors of the Federal Reserve System
- Office of the Comptroller of the Currency (OCC)
  regulated banks

Recent Board Developments

MSRB's Board has both representatives from regulated entities that it is required to regulate and public representatives. Recently, there have been structural changes implemented at the Board level. See "Notable Recent Observations – Governance/Compliance Developments – MSRB" below.

Best Judgment Standard
Municipal Securities

General

MSRB Rule G-13 requires that dealers, brokers or their authorized agents use their "best judgment" when quoting prices related to municipal securities.

Indicators that a price quotation is in the broker/dealer's "best judgment" include a price quotation's reasonable relationship to the fair market value of the securities at the time the quotation is made. According to an April 1988 MSRB interpretation of Rule G-13, relevant factors for municipal security price quotations include a dealer's (i) current overall and security-specific inventory position, and (ii) anticipation of the market price for the securities. Finally, a broker or dealer would be acting outside of its best judgment if it is not prepared to buy or sell the securities at the price published.

Violations

Responding to concerns about the meaning of "best judgment" and its practical application, the MSRB provided the following three examples of how to operationalize the best judgment rule (the " MSRB 1977 interpretation letter") :

Bid Restrictions – Bonds Subject to Redemption
In the first example, a dealer who knowingly submits a bid for general market bonds that have been called by the issuer, at a price more appropriate for bonds not subject to redemption, is acting "unethically." Such actions would run afoul of the "free and open" nature of municipal securities markets. In that same example, should a dealer on the other side of a trade accept the bid, this dealer arguably is acting outside of its best judgment because it is presumed to be aware of the bonds' called status. Although such a transaction between professionals would be insufficient to sustain a fraud charge, the acceptance of the trade would not relieve the bid-making dealer from a MSRB Rule G-13 enforcement action.

Bond Valuation Mismatches
A dealer who submits a bid for bonds based on valuations from independent sources that mistake the

nature of the proffered securities is the second example of an action outside of the best judgment rule. Under these circumstances, if the dealer knew that the valuation was mistaken, its bidding would also violate this rule [4].

Lack of Any Dealer Diligence
Finally, a dealer who makes a bid or an offer on a security, having no knowledge of the value of the security or of comparable securities, is the third example of a situation where MSRB would likely recommend that an enforcement action be brought against a broker or dealer. MSRB specifically stated that a price quotation that is "pulled out of the air" is not based on the dealer's best judgment and is against the promotion of free and open markets in municipal securities.

Corporate Securities

Best Execution

Pursuant to FINRA Rule 5310, a broker-dealer or broker is required to use reasonable diligence to ascertain the best market for the subject security and buy or sell in such market so that the resultant price to the customer is as favorable as possible under prevailing market conditions.

Parallel provisions are contained in MSRB Rule G-18.

Fair Quotations

Generally, under FINRA Rule 5220 and MSRB Rule G-13(b), no broker-dealer may make an offer to buy or sell a security at a stated price unless a bona fide price and the broker-dealer is prepared to purchase or sell at such price and at such conditions stated at the time of such offer.

Suitability
A broker-dealer must have a reasonable basis to believe that a recommended transaction or investment strategy is suitable for a customer, both from a municipal and a corporate perspective. This is to be based upon the reasonable diligence of the broker-dealer including, but not limited to, investment objectives, and experience, liquidity needs, and risk tolerance.

Fair Dealing Requirement
Municipal Securities

General

Under MSRB Rule G-17, which regulates conduct of municipal securities and municipal advisory activities, each broker, dealer and municipal advisor has a duty to deal fairly with all persons. This rule prohibits any deceptive, dishonest or unfair practices.

MSRB Rule G-17 contains for applying the rule in various contexts. These notices include guidance on use of the rule as a remedy for actions such as: (i) delaying delivery of securities to customers (October 13, 1983); (ii) conduct of syndicate managers (on selling short, December 21, 1984); (iii) altering settlement issue dates (February 26, 1985); (iv) charging excessive fees (July 29, 1985); (v) disclosure obligations of prepayment of principal (March 19, 1991); (vi) disclosure of material facts (on original issue discount bonds, January 5, 2005); (vii) bond issue ratings (January 22, 2008); and (viii) protection of municipal entities (August 2, 2012).

The rule provides that customers or other parties harmed by violations of MSRB Rule G-17 may seek recovery through MSRB's arbitration program or through litigation.

Recent Effectiveness of Fair Dealing Interpretive Notice

General

Importantly, the aforementioned interpretive notice relating to the protection of municipal entities was amended on November 6, 2019, with an effective date of November 30, 2020. It was subsequently amended on February 16, 2021, with an extended effective date of March 31, 2021 (the "2021 Fair Dealing Interpretive Notice"). It noted that the prior interpretative notice, dated August 2, 2012, and related interpretations (collectively, the "2012 MSRB G-17 Interpretative Notic e") will only apply to prior underwriting relationships.

The 2021 Fair Dealing Interpretive Notice states that MSRB Rule G-17 does not merely prohibit deceptive conduct on the part of the registered broker-dealer and broker, but also establishes a general duty to deal fairly with all persons including, but not limited to issuers, *even in the absence of fraud*.

Lack of Fiduciary Duty

However, a broker-dealer does not have a fiduciary duty to the issuer under Federal securities laws and, therefore, is not required to act in the best interests of the issuer without regard to its own financial or other interests. Consequently, the broker-dealer may not discourage issuers from retaining a municipal advisor or otherwise imply that hiring a municipal advisor is redundant as the municipal advisor, unlike the broker-dealer, does have a fiduciary duty to the issuer. [5]

Required Transaction-Specific Disclosures

A broker-dealer is required to deliver transaction-specific disclosures where it has recommended a financing structure or product to an issuer. Such disclosures are to be specific rather than general in nature and, among other things, be based upon the type of structure or product recommended, as well as the issuer's knowledge and experience regarding such structure or product.

Additional Complex Municipal Securities Requirements

In the 2021 MSRB G-17 Interpretive Notice complex municipal securities, financing requires even more particularized transaction-specific disclosures than do routine financing structures or products. Complex municipal securities financings include, but are not limited to, variable rate demand obligations (VRDOs), financings involving interest rate swaps and financings in which interest rates are benchmarked to an index (e.g. LIBOR, SIFMA or SOFR). The fact that a structure or a product has become relatively common in the market does not reduce its complexity.

Specifically, the broker-dealer must disclose the related material characteristics and material financial risks of this type of complex municipal securities structure or product to the issuer. By way of example, for an interest rate swap, such disclosures include: (i) the material characteristics such as material economic terms, material operational issues, and material rights and obligations of the parties, and (ii) the material financial risks such as market, credit, operational and liquidity risks.

Such disclosures should be sufficient to allow the issuer to assess the magnitude of its potential exposure, and that there may be accounting, legal and other associated risks. The 2021 Fair Dealing Interpretive Notice also notes that such a registered entity may also be subject to Commodity Futures Trading Commission (CFTC) and SEC rules.

In addition, any incentives the broker-dealer receives in recommending a complex municipal securities financing must be disclosed.

Conduit Borrower Obligation

Notably, the 2021 Fair Dealing Interpretive Notice does not set out the broker-dealer's duties to other parties to a municipal securities financing such as conduit borrowers, but notes that MSRB Rule G-17 requires that an underwriter deal fairly with all persons involved in the financing.

Corporate Securities

General

To supplement FINRA Rule 2010, FINRA has a general rule that a registered broker-dealer or broker cannot effect any transaction in, or induce the purchase or sale of, any security by any manipulative, deceptive or other fraudulent device or contrivance.

Additional Complex Corporate Securities Requirements

As with municipal securities, FINRA has additional requirements for complex securities such as interest rate swaps. However, these requirements are tied into a registered entity's suitability obligations under FINRA Rule 2111.

Supervision

Municipal Securities

MSRB Rule G-27, focusing on supervision, creates an obligation on the part of brokers and dealers to supervise certain activities in order to ensure compliance with MSRB Rules and the Securities Act of 1933, as amended, and to establish a system of supervision of the municipal securities activity of each dealer and certain related employees. The supervisory procedures must be in writing, contain instructions for regular internal inspections of activities – with the goal of detecting and preventing violations of the applicable rules – and include instructions for the review of incoming and outgoing correspondence of its municipal securities representatives.

Finally, each dealer is required to designate a principal to establish, maintain and enforce supervisory control policies and procedures that comport with the municipal securities activities of the dealer, in addition to the specific procedures required in para. (f) of the rule. MSRB Rule G-27's interpretations address questions regarding who may be designated with supervisory responsibilities (branch office managers, municipal securities principals and sales principals) and procedures for review of correspondence with the public. Additional clarifications are laid out in interpretive letters.

Corporate Securities

Generally, the registered broker-dealer or broker must (i) designate chief compliance officers and (ii) have in place processes to establish, maintain and review policies and procedures reasonably designed to achieve compliance with applicable FINRA Rules and Federal securities laws and regulations.

The broker-dealer's supervisory system must provide, among other things: (i) written procedures, (ii) designation of an appropriately registered principal with authority to carry out the supervisory responsibility for (a) each type of business requiring registration and (b) each supervisory jurisdiction/branch office, (iii) assignment of each registered person to an appropriately registered representative or principal who is to be responsible for supervision of said person's activities, (iv) internal inspections and (v) importantly, a review and investigation of transactions that are reasonably determined to violate the Securities Exchange Act of 1934, as amended, or FINRA Rules prohibiting manipulative and deceptive devices.

Notable Recent Observations

Governance/Compliance Developments

MSRB

At the end of December 2019, *The Bond Buyer* reported that many of its senior officials left the MSRB during 2019 including its Chief Executive Officer, Chief Regulatory Officer and General Counsel. Starting in Fall 2020, these officers were replaced. One of the examination priorities of the SEC's Division of Examinations is the effectiveness of MSRB's policies, procedures and controls.

In Fiscal Year 2021, the MSRB implemented certain structural changes to its Board including, among other things (i) tightening the independence standard of public representatives on the Board by requiring a minimum of five (5) years (versus two (2) years) of separation from a regulated entity; (ii) splitting its Nominating and Governance Committee into two (2) separate committees – one focusing on Board nominations and the other focusing on Board governance; (iii) requiring that the chair of its Nominating, Governance and Audit Committees be public representatives and not regulated entity representatives from the Board, and (iv) the re-establishment of two advisory groups – the Compliance Advisory Group and the Municipal Fund Securities Advisory Group.

At its recent quarterly board meeting, the MSRB (i) selected a new Chair, (ii) announced that the Chief Risk Officer will assume the Chief Financial Officer role from the Chief Operating Officer who had a dual role, presumably leaving a vacancy in the Chief Risk Officer role, and (iii) stated it will soon announce the names of four (4) new board members to start on October 1, 2021. The new MSRB board members were announced on August 4, 2021.

Broker-Dealers

It should be noted that some of the largest banks have recently replaced their Chairs, Chief Executive Officers, Chief Compliance Officers and Chief Risk Officers. [6]

SEC

As part of the 2021 Examination Priorities, the Division of Examination also highlighted (i) the importance of internal compliance programs and Chief Compliance Officers at regulated entities, (ii) broker-dealer rules, in both the corporate and municipal bond markets, relating to best execution, pricing and mark-ups, (iii) Reg BI compliance and whether registered investment advisors have fulfilled their fiduciary duties of care and loyalty to their clients, and (iv) in the municipal securities area, whether municipal advisors have met their fiduciary duty obligations to municipal entity clients, including the disclosing of and managing of conflicts of interest and documentation of the scope of their client engagements.

FINRA Arbitration Requirements

FINRA recently reminded its member firms about requirements when using pre-dispute arbitration agreements for customer accounts. In particular, it noted that FINRA Rules do not allow class action claims in arbitration, specifically restricting members' actions preventing customers from bringing or participating in judicial class actions by adding class action waivers in these pre-dispute arbitration agreements.

As FINRA is by far the largest dispute forum for the U.S. securities industry, this is an important protection for investors.

Regulation Best Interest (Reg BI)

Corporate Securities

Adopted by the SEC in 2019, the Regulation Best Interest rule set a new standard of conduct for broker-dealers and their associates that go beyond the existing suitability obligations in FINRA Rule 2111. Reg BI requires that broker-dealers and their associates act in the best interest of a retail customer when making recommendations for any securities transaction or an investment strategy involving securities. Reg BI is not applicable to commercial customers.

Incorporating the care and conflict of interest obligations, and other key principles in the fiduciary duties of care and loyalty under Section 206(1) and (2) of the Investment Advisers Act of 1940, as amended, the goal of Reg BI is to align the broker-dealer standard of conduct with the reasonable expectations of retail customers. Two main indicators that a broker-dealer is acting in the best interest of its retail customers are: (i) making recommendations that do not prioritize the interest of the broker-dealer or its firm ahead of the interests of the retail customer; and (ii) establishing, maintaining and enforcing policies and procedures aimed at facilitating full and fair disclosure of any conflicts of interests.

The rule notes that disclosure is insufficient to meet the standard of conduct established by Reg BI.

Municipal Securities

In March, the MSRB indicated that the Reg BI principles would soon apply to bank dealers whose retail investment products and offerings include municipal securities. This is important as over two-thirds of municipal securities are held by individual investors either directly or through mutual funds.

Rules Equally Applicable to Corporate Bond Market

Although the instant case related to bidding on municipal securities, parallel rules apply to the corporate bond market as highlighted above.

To Enforce or Not to Enforce

Enforce

Enforcement of the rules set forth in this *Client Alert*, and other existing rules by the SEC, FINRA and the MSRB, is critical for the proper functioning of both the municipal and corporate bond markets. This will ensure the fair, transparent and efficient operations of these essential financial markets.

Not to Enforce

On the other hand, as quoted in the previously mentioned Bond Buyer article with respect to FINRA's enforcement action of the best judgment standard that is the first legal topic of this Client Alert, a representative of Bond Dealers of America [7] stated that:

> *One of our concerns is that this case could establish compliance standards for the market more broadly. We don't have any problems with compliance standards, but enforcement cases are not the way to establish compliance standards.*

Answer to the Question

We leave it to the reader to decide which is the best path to assure compliance with the applicable

MSRB and FINRA Rules, and related supervision standards, in the municipal bond and corporate securities markets.

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[1] During the publication of this writing, our prediction rang true. In late August, the SEC fined a firm and its former CEO for failing to disclose conflict of interest.

[2] See MSRB Interpretation of February 24, 1977 of MSRB Rule G-13 MSRB 1977 Interpretation Letter, citing the Senate Report 94-75, 94th Cong., 1st Sess., 42-32.

[3] This bankruptcy caused a significant delay of the lead author's simultaneous pricing of life care facility bonds issued by Orange County, New York.

[4] Although not addressed in the MSRB 1977 Interpretation Letter, it is our belief that the best judgment rule would also be violated, if based upon reasonable diligence, the dealer should have known that the valuations were erroneous.

[5] The fair dealing rule, MSRB Rule G-17, relates to both solicitor municipal advisors (those who solicit on behalf of third-parties such as broker-dealers) and non-solicitor municipal advisors. In addition, a new draft rule highlights that solicitor municipal advisors, as compared to non-solicitor municipal advisors, do not have a fiduciary duty to municipal entities and conduit borrowers but are required to (i) have a reasonable basis for their representations, (ii) refrain from making misrepresentations that they know or should know are inaccurate or misleading, (iii) disclose material facts about (a) its role, compensation and conflicts of interest, and (b) the broker-dealer or other third-party that the solicitor municipal advisor represents including, but not limited to, such party's disciplinary history. See MSRB Notice 2021-07 dated March 17, 2021, with a comment deadline of June 17, 2021, relating to draft MSRB 'Rule G-46 – Duties of Solicitor Municipal Advisor s.' Comments to draft MSRB Rule G-46 were received from the following associations: (i) National Association of Municipal Advisors (NAMA), (ii) Securities Industry and Financial Markets Association (SIFMA), the leading trade association for broker-dealers, investment banks and asset managers operating in the US and global capital markets according to its website, and (iii) Third Party Marketers Association (3PM). NAMA recommends that MSRB require solicitor municipal advisors to disclose to the municipal entities they are soliciting, as well as conduit borrowers, that they do not have a fiduciary duty to them. SIFMA, among other things, suggests that a clear statement be made in the draft rule that 'solicitor municipal advisors do not owe a fiduciary duty to their clients and solicited entities.' In addition, SIFMA questions why representations made by a solicitor municipal advisor 'must be truthful and accurate' as it believes it is inconsistent with what non-solicitor municipal advisors must comply with.
Among 3PM's comments, it suggests that MSRB should not apply draft Rule G-46 to conduit borrowers, or provide guidance to solicitor municipal advisors that are also municipal advisor third-party solicitors working on behalf of third-party investment advisors.

[6] Since 2020, the following senior managers had resigned: Citigroup (Chief Executive Officer, Chief Compliance Officer and Chief Risk Officer), Credit Suisse (Chair, Chief Compliance Officer and Chief Risk Officer), Deutsche Bank (Chief Compliance Officer and Chief Risk Officer), Goldman Sachs (Chief Compliance Officer), HSBC (Chair, Chief Compliance Officer and Chief Risk Officer), Lloyds Bank (Chair), and Wells Fargo (Chief Compliance Officer and Chief Risk Officer). In addition, there were significant senior leadership changes announced at Bank of America in August/September 2021 including: (i) departures of Vice Chairman, Chief Operating Officer, and Head of Fixed Income, Currencies and Commodities Sales/CEO of BofA Securities Europe SA/Country Executive for France, with no replacements yet determined, (ii) departure of Global

General Counsel with a replacement announced, (iii) internal position changes of Chief Financial Officer, Chief Administrative Officer, President of Global Commercial Bank and Business Banking, and President of Retail Banking, (iv) the split of the Chief Operations and Technology Officer role into two roles – Chief Technology and Information Officer, and Chief Operations Executive, and (v) new positions created for Global Compliance and Operational Risk, and Global Real Estate and Business Continuity.
Also in 2021 (i) JPMorgan Chase & Co. (a) announced the resignation of the Co-President and Chief Operating Officer, and (b) included as new members to its Operating Committee: the Global Head of Securities Services, Executive Chair of Investment Banking & Corporate Banking, and Head of Global Markets, and (ii) Mizuho Financial Group announced changes in senior management for the Group, Mizuho Bank and Mizuho Securities.

[7] According to Bond Dealers of America, it is the only trade association exclusively focused on U.S. fixed income markets and represents bond dealers headquartered in cities across the country.

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by Kirsten Hart, Patrice Howard, Ph.D., Les Jacobowitz

September 22, 2021

Arent Fox

SEC Charges School District with Misleading Bond Investors.

The Securities and Exchange Commission (SEC) has charged a San Diego County-based school district and its former chief financial officer with misleading investors who purchased $28 million in municipal bonds.

The SEC's complaint alleges Sweetwater Union High School District and the school district's former CFO, Karen Michel, gave investors misleading budget projections indicating the school district would be able to cover its costs and end the fiscal year with a general fund balance of approximately $19.5 million.

However, the SEC maintains the school district was involved in deficit spending en route to a negative $7.2 million ending fund balance.

Additionally, the SEC indicated the Sweetwater Union High School District, without admitting or denying any findings, agreed to settle with the SEC and consented to the entry of an SEC order finding that it violated two Sections of the Securities Act and would engage an independent consultant to evaluate policies and procedures related to its municipal securities disclosures.

The SEC noted Michel, without admitting or denying the allegations in the agency's complaint, agreed to settle with the SEC and be enjoined from future violations of the charged provision, as well as from participating in any future municipal securities offerings while agreeing to pay a $28,000 penalty. The settlement is subject to court approval, per authorities.

"As the order finds, Sweetwater and Michel presented stale and misleading financial information as current and accurate," LeeAnn G. Gaunt, chief of the Division of Enforcement's Public Finance Abuse Unit, said. "The SEC will continue to address deceptive conduct that prevents municipal bond

investors from getting an accurate picture of the financial risks of their investments."

FINANCIAL REGULATION NEWS

BY DOUGLAS CLARK | SEPTEMBER 20, 2021

Firm Settles SEC Charges For Prioritizing "Flippers" In Municipal Offerings: Cadwalader

In separate Orders, a municipal securities firm, the head of the firm's sales, trading and syndication group, and the head of the firm's syndicate desk settled SEC charges (see here, here, and here, respectively) for inappropriately allocating municipal bonds to "flippers" (i.e., unregistered brokers that buy and sell bonds at a profit).

The SEC found that between January 2014 and December 2017 the firm failed to follow its "standard methodology" when serving as a sole underwriter or senior syndicate manager in negotiated offerings in which it allocated bonds. The SEC stated that the firm's methodology required it to prioritize the fulfillment of customer, dealer, syndicate member and other broker-dealer orders over flipper orders.

The SEC found that:

- on 41 separate occasions, the firm did not prioritize institutional customer or dealer orders over flipper orders, even when it had more orders than available bonds;
- on three separate occasions, the firm knowingly did not allocate bonds per issuer instructions, offering them to flippers before retail customers; and
- in instances in which the firm did not act as a participating underwriter, it caused flippers to act as unregistered broker-dealers by acquiring new issue municipal bonds from the flippers and compensating them on the basis of the transactions.

In addition, the SEC determined that both the head of the firm's sales desk and the head of the syndicate desk were aware of the improper conduct.

The SEC found that the respondents violated MSRB Rules G-11(k) ("Retail Order Period Representations and Required Disclosures") and G-17 ("Conduct of Municipal Securities and Municipal Advisory Activities") and Section 15B(c)(1) ("Discipline of municipal securities dealers; censure; suspension or revocation of registration; other sanctions; investigations") of the Exchange Act. In addition, the SEC found that the firm violated MSRB Rule G-27 ("Supervision") and caused violations of SEA Section 15(a)(1) ("Registration of all persons utilizing exchange facilities to effect transactions; exemptions").

To settle the charges, respondents agreed to (i) a censure, (ii) cease and desist from future violations, and (iii) $150,000, $30,000 and $25,000 civil money penalties, respectively, of which a portion will be sent to the MSRB. The firm also agreed to pay $713,327 in disgorgement and prejudgment interest.

by Cadwalader, Wickersham & Taft LLP

22 September 2021

NFMA Accepting Applications for At-Large Seats on the 2022-2023 Board of Governors.

We are accepting applications for At-Large seats on the 2022-2023 Board of Governors

Applications are due by October 1, 2021. To apply, click here.

Please contact Lisa Good at lgood@nfma.org if you have questions.

RBC Capital Settles with SEC for $800K Over Muni Bond Dealings.

RBC Capital Markets has agreed to pay more than $800,000 to settle charges that the firm engaged in unfair dealing in municipal bond offerings, according to the Securities and Exchange Commission.

The SEC alleges that between January 2014 and December 2017, RBC Capital Markets allocated bonds meant for institutional customers and dealers to unregistered brokers known as “flippers,” according to an SEC order published on Friday last week. The flippers, in turn, sold the bonds to other broker-dealers at a profit, according to the SEC.

RBC Capital Markets agreed to the censure and to pay $863,326 without admitting or denying the SEC’s findings. The amount included a $150,000 penalty, disgorgement of $552,440 and prejudgment interest of $160,886, according to the SEC.

In three specific instances, the SEC said RBC Capital Markets went as far as to violate instructions from an issuer that the firm prioritize retail customers first and that “RBC knew or should have known that flippers were not eligible for retail or institutional priority.”

“RBC improperly acquired new issue municipal bonds for the firm’s inventory by placing orders with the flippers to circumvent the lower priority that issuers typically assigned to non-syndicate dealer orders in offerings that it did not underwrite,” according to the SEC order.

RBC Capital Markets is registered with the SEC as a broker-dealer, municipal securities dealer, investment advisor and municipal advisor.

The municipal bond offering violations are among the SEC’s focus areas. The regulator says it has taken action against municipal bond offering flipping and other retail order period violations eight times since August 2018, including in July 2020 when it ordered UBS Financial Services to pay $10 million over similar allocation violations, which the firm agreed to do without admitting or denying the findings.

SEC Orders UBS to Pay $10M for Violating Municipal Bond Offering Rules
“We will continue to pursue those who undermine priority rules and crowd out legitimate retail or institutional customers from getting access to newly issued municipal bonds,” LeeAnn Gaunt, chief of the SEC division of enforcement’s public finance abuse unit, said in a statement.

Separately, the SEC issued orders against former RBC Capital Markets head of municipal sales, trading and syndication Kenneth Friedrich and the head of its municipal syndicate desk, Jaime Durando. The agency said that Friedrich and Durando “permitted the improper allocation and sale of

new issue bonds to the flippers, and that Friedrich also permitted the improper purchase of new issue bonds for RBC's own inventory through the flippers."

Friedrich and Durando each agreed to a censure and to pay $30,000 and $25,000, respectively, according to the SEC. Friedrich also consented to a six-month limitation on supervisory activities and a six-month prohibition on trading negotiated new issue municipal securities.

Friedrich was registered at RBC Capital Markets from 1999 to 2017, while Durando has been at registered at the firm since 2006, according to their BrokerCheck records.

Financial Advisor IQ

By Andrew Kessel

September 20, 2021

Amendments to Rule G-10 Notification Requirement for Dealers: SIFMA Comment Letter

SUMMARY

SIFMA submitted comments to the Securities and Exchange Commission ("SEC") on the Municipal Securities Rulemaking Board's ("MSRB's") Filing of a Proposed Rule Change Consisting of Amendments to Rule G–10, on Investor and Municipal Advisory Client Education and Protection, and Rule G–48, on Transactions With Sophisticated Municipal Market Professionals, To Amend Certain Dealer Obligations (the "Filing").

SIFMA supports many elements of the proposed amendments, which reduce the compliance burden on the dealer community without reducing investor protections. The proposed amendments will render potential cost savings, and each customer notification that no longer needs to be printed or mailed will reduce the environmental impact of this process.

Read the Comment Letter.

SEC Approves MSRB Extension for Municipal Advisor Principal Qualification Examination: Cadwalader

The SEC approved an MSRB proposal to extend the deadline for a municipal advisor principal to become qualified by passing the Series 54 examination on line. As a result, the deadline was extended from November 12, 2021 to November 30, 2021.

The extended deadline "roughly coincides with the number of days taken to launch the Series 54 examination online" and is effective immediately. Comments on the extension must be submitted by October 7, 2021.

September 16 2021

Cadwalader Wickersham & Taft LLP

A Big Bond Market Headache, Courtesy of the SEC.

Chair Gary Gensler wants to bring greater efficiency and transparency to debt trading, but an updated rule could do just the opposite.

U.S. Securities and Exchange Commission Chair Gary Gensler made waves in the fixed-income market earlier this week, signaling that he wants to find ways to "bring greater efficiency and transparency" to trading debt.

Yet beneath the surface, the regulator is just days away from potentially causing serious disruptions in those same bond markets.

An obscure SEC rule, 15c2-11, was amended a year ago for the first time in almost three decades. The change, which is meant to improve disclosure and investor protection in over-the-counter trading markets, sounds innocuous enough on its face. It ensures "that broker-dealers, in their role as professional gatekeepers to this market, do not publish quotations for an issuer's security when current issuer information is not publicly available."

There's one big problem: The rule, which had long been understood to safeguard retail investors from penny stocks and other "pump-and-dump" schemes, doesn't explicitly exclude fixed-income assets, except for municipal bonds. The Bond Dealers of America, a trade association for securities dealers and banks specializing in fixed income, says SEC staff have informally confirmed that the rule applies equally to both equities and debt.

"The industry is mildly freaking out," Kevin McPartland, head of research in Greenwich Associates' market structure and technology group, said in an interview. Firms must be compliant with the amendment on Sept. 28. "Dealers can't operationally make that happen in that span of time. If nothing changes, at the end of the month they may have to stop quoting some bonds," he said.

To get a sense of the level of panic, look no further than an Aug. 6 joint letter from the Securities Industry and Financial Markets Association and the BDA, which are seeking an exemption:

> "We are concerned that the rule as written could apply broadly to quotation activity for fixed income securities, and that the application of the rule to quotations for fixed income securities will deter that quotation activity in a way that will have a significant, deleterious effect on the fixed income markets. We believe that such an application of the rule is overbroad and unnecessary and will increase costs, decrease liquidity, and reverse the gains in transparency that the fixed income markets have achieved in recent years as the market has become more electronic."

In other words, this rule change could do precisely the opposite of what Gensler was advocating for in his prepared remarks before the Senate Banking Committee.

An earlier letter in May from the BDA details how it would affect certain corners of the bond market. Non-government guaranteed mortgage-backed securities, for instance, are issued through trusts, meaning each transaction is unique. Under the amended rule, traders would have to review updates to each underlying pool of mortgages if they wanted to quote a price for a bond. Another example: A security is exempt from the rule if its average daily trading volume is at least $100,000 during the 60 calendar days before giving a price quote. That might save benchmark bonds from AT&T Inc.,

General Electric Co. and Microsoft Corp., but it could paralyze the secondary market for high-yield debt, where companies are more often private, smaller and opaque.

Throughout the letter, the BDA can barely hide its incredulity at the whole situation. The group summarizes its position like this:

> "The bond market simply is not the high risk, low transparency world of microcap stocks. Moreover, applying the Rule to fixed income would increase compliance costs for dealers, which ultimately would be reflected in higher transaction costs for investors. Finally, adding additional requirements before a firm can provide a quote or execute a trade for a customer could discourage firms from quoting certain securities altogether."

As far as I can tell, this looming compliance headache hasn't been discussed much anywhere, aside from these letters. That's likely because bond traders assumed the SEC couldn't possibly have intended to rope mortgage-backed securities and junk bonds into its Exchange Act Rule 15c2-11, given the gigantic size of those markets relative to a few hundred thinly traded stocks. Yet for now, that's exactly what it's doing.

"Until April of this year, I've never paid attention to this rule because this was not a fixed-income rule," Michael Decker, the BDA's senior vice president of federal policy and research, said in an interview. "The SEC has now taken the position that the rule already applies to fixed income and it has always applied."

The rule was changed when Jay Clayton was the head of the SEC. In a statement announcing the amendment, he applauded the long-overdue shifts to address fraud in markets with significant amounts of retail investors. That sure doesn't sound much like private-label MBS and high-yield debt, which are dominated by institutions.

"I don't think the SEC has thought through this," Decker said. In light of Gensler's recent remarks, " it's wise for everybody to take a few steps back, think about what enforcement policies will look like."

An SEC spokesperson didn't reply to an emailed request for comment.

Bloomberg Markets

By Brian Chappatta

September 16, 2021

Gensler Turns Spotlight on How Hard It Can Be to Get Bond Prices.

- **SEC chair wants to 'bring greater efficiency and transparency'**
- **Fed's pandemic bond market rescue a source of concern**

After U.S. Securities and Exchange Commission Chairman Gary Gensler signaled he may overhaul bond market regulations, industry experts zeroed in on just how opaque trading can be.

Gensler, who testified Tuesday before the Senate Banking Committee, said in prepared remarks released beforehand that he wants to "bring greater efficiency and transparency" to the trading of

corporate bonds, municipal bonds and mortgage-backed securities. He offered little detail on what new rules might look like.

Market watchers have suggestions, a year after a liquidity breakdown early in the pandemic forced the Federal Reserve to backstop the bond market. A big source of angst: especially when compared with other key financial assets like stocks, it can take a lot more effort to figure out the price of a bond.

“Pre-trade transparency is a focus,” said Kumar Venkataraman, a finance professor at Southern Methodist University and former member of the SEC’s Fixed Income Market Structure Advisory Committee. “If you’re a large, sophisticated investor, you receive quotes from many dealers and see the best price. If you’re less sophisticated, you might get a less competitive bid.”

15 Minutes

Currently, corporate bond trades must be reported to the Financial Industry Regulatory Authority’s Trace system no more than 15 minutes after they’re executed — a deadline that feels like an eternity in the era when stock and futures traders fret about microseconds.

And before trades are placed, there are no publicly available price quotes. To get those can require making phone calls or sending electronic requests for quotes to a bunch of banks and brokers.

A potential solution would require bond brokers to report their offered prices to a centralized system, which is how it’s worked in the U.S. stock market since the 1970s. That could make the business more efficient by stitching together all the different markets where bonds trade. In stocks, for instance, all orders are supposed to be automatically routed to the market with the best price.

“We think the solution is to consolidate all credible bids and offers into a central system and display that information publicly,” said Christopher White, the chief executive officer of bond market data provider BondCliQ Inc. “Once you create that centralized architecture, you start to see the quality of the data and the market improve.”

Sell-side banks have little incentive to provide greater transparency, since it could cut into their profits. And reporting quotes could be a costly and time-consuming process that banks currently have little interest in participating in, Venkataraman said.

Don’t expect corporate bonds to begin trading in a centralized system like equities anytime soon, says Kevin McPartland, head of research for market structure at Coalition Greenwich.

‘Very Different’ Market

“The bond market is still very different from the equity market in terms of how it trades and in terms of the market participants,” he said. “Bond markets are by and large institutional markets. So we have a very informed consumer if you will.”

There is also “post-trade reporting, and a lot of private sector work to improve pre-trade price transparency,” he added. “The buy side has pushed for it, and the platforms and data providers have really pushed to make pre-trade price transparency better. So I’m not sure we need to regulate something that’s effectively already happening.”

The bond-market crisis of March and April 2020 is fresh in regulators’ minds. Government officials appear to view the unprecedented steps taken by the Fed in March 2020 as a mandate to address long-standing concerns that bond liquidity disappears in bad times.

The giants of finance, meanwhile, are more apt to view the global pandemic as a once-in-a-century event that doesn't justify upending how the corporate bond business runs in normal environments.

Gensler has targeted market transparency before. The opacity of the swaps market was one of the reasons why the 2008 financial crisis was so severe, since it was extremely difficult to untangle the connections between Wall Street banks who held the derivatives. Gensler, as chairman of the U.S. Commodity Futures Trading Commission, oversaw a push to get more of that business done on public markets.

Bloomberg Markets

By Jack Pitcher

September 14, 2021, 11:35 AM MDT

U.S. SEC Chair Wants Private Fund Fee Disclosures, Bond Market Transparency - Testimony

WASHINGTON (Reuters) – The chair of the top U.S. securities regulator wants private funds to disclose more information to investors about potential conflicts of interest and the fees they charge, according to congressional testimony published Monday evening.

Gary Gensler, chair of the Securities and Exchange Commission (SEC), also wants to impose greater transparency on the corporate bond, municipal bond and asset-backed securities market, which combined are worth about $28 trillion, he wrote in the testimony submitted to the Senate Banking Committee.

Gensler will appear before the congressional panel on Tuesday to field questions on his agenda for the regulator.

"I believe we can enhance disclosures in this area, better enabling pensions and others investing in these private funds to get the information they need to make investment decisions," Gensler wrote.

In the bond markets, meanwhile, trading data is often insufficient, causing liquidity crunches during times of stress, which was evident during last year's market turmoil sparked by the COVID-19 pandemic.

"This market is so critical to issuers. It is nearly 2.5 times larger than the commercial bank lending of about $10.5 trillion in our economy," Gensler wrote in his testimony, without elaborating on the changes he may pursue.

Addressing fund fees and the bond market add to an already jam-packed agenda for the SEC, which is working on new corporate climate change-risk disclosures, cracking down on blank-check company deals, and overhauling several aspects of the U.S. equity market structure.

Also on Monday, Gensler, writing in a Wall Street Journal op-ed, urged Chinese companies to open up their books and records to SEC scrutiny or risk being kicked off U.S. exchanges.

(Writing by Michelle Price; Editing by Leslie Adler)

September 13, 2021

SEC Charges High School District CFO with Misleading Investors.

Dive Brief:

- The Sweetwater Union High School District and its former CFO, Karen Michel, settled claims that they misled investors in a $28 million municipal bond offering, the Securities and Exchange Commission says.
- The SEC alleged that Michel and the Chula Vista, Calif.-based school district, in San Diego County, gave investors misleading budget projections and hid the fact that its finances "were severely strained."
- Michel and the public school district said the district would conclude 2021 with $19.5 million in its general fund, the SEC alleges, but later revealed that the school had overspent its budget by $28 million, resulting in a year-end deficit of $7.2 million.

Continue reading.

CFO Dive

by Jane Thier

Sept. 17, 2021

SEC Reaches Settlements with Sweetwater Union District, Ex-CFO for Filing False Reports.

CHULA VISTA, Calif. (CNS) – The Securities and Exchange Commission announced Thursday that it has entered into a settlement agreement with the Sweetwater Union High School District and its former Chief Financial Officer to resolve allegations that the district misled investors who purchased $28 million in municipal bonds.

The SEC alleged that in 2018, the school district and former CFO Karen Michel gave investors misleading budget projections indicating it would end the fiscal year with a general fund balance of around $19.5 million when it was actually on track for a negative $7.2 million ending fund balance.

The agency said that despite contradictory internal reports, the district and Michel included the projections in its offering documents and presented them to a credit rating agency. Michel also signed "multiple certifications falsely attesting to the accuracy and completeness of the information included in the offering documents," the SEC said.

While neither settlement includes admissions or denials of the SEC's allegations, Michel agreed to settle with the SEC and pay a $28,000 penalty, while the district entered into an SEC order that requires it to retain an independent consultant to evaluate and make recommendations to its procedures regarding its municipal securities disclosures.

When reached for comment, the school district said in a statement, "The district looks forward to

implementing the improvements and changes outlined in the SEC's order. It will continue to take steps to ensure it provides accurate disclosures and information to the public."

The district's statement also said the settlement "represents another positive step in the district's ongoing remedial efforts to continuously evaluate and improve its fiscal health."

LeeAnn G. Gaunt, chief of the SEC's Public Finance Abuse Unit, said, "As the order finds, Sweetwater and Michel presented stale and misleading financial information as current and accurate. The SEC will continue to address deceptive conduct that prevents municipal bond investors from getting an accurate picture of the financial risks of their investments."

fox5sandiego.com

Sep 16, 2021

SEC Settles with San Diego-Area School District and Former CFO.

The Securities and Exchange Commission has settled with Sweetwater Union High School District in San Diego County, California, as well as its former chief financial officer Karen Michel for misleading investors in connection with an issuance of $28 million of municipal bonds.

The Commission charged Michel with violating Section 17(a)(3) of the Securities Act of 1933, and she agreed without admitting or denying the allegations to pay a $28,000 penalty. She is barred from participating in future municipal securities offerings and agreed to refrain from future violations.

Sweetwater, without admitting or denying guilt, violated Sections 17(a)(2) and 17(a)(3) of the Securities Act, the SEC said, and is required to convene with an independent consultant to evaluate its policies and procedures in relation to its municipal securities disclosures.

"As the order finds, Sweetwater and Michel presented stale and misleading financial information as current and accurate," said LeeAnn G. Gaunt, chief of the division of enforcement's public finance abuse unit. "The SEC will continue to address deceptive conduct that prevents municipal bond investors from getting an accurate picture of the financial risks of their investments."

Michel, who worked within Sweetwater Union High School District's financial services department from 1996 to 2018, failed to accurately budget for a 3.75% pay raise approved shortly before the beginning of the 2018 fiscal year, the SEC found.

Instead of adding these increases to the district's expenses, Michel allegedly instead projected expenses nearly identical to the expenses incurred during the 2017 fiscal year, which took into account a less than 1% increase in employee compensation.

The Commission also found that despite Sweetwater's mid-year budget monitoring reports consistently showing higher expenses than the previous year, Michel made no effort to bring its budget in line with the actual expenses.

The April 2018 $28 million bond offering documents then included misleading budget projections

which indicated the district could cover its costs and would end the year on June 30, 2018 with a general fund balance of $19.5 million, when in reality it ended the year with a negative $7.2 million balance.

After Michel's retirement in September 2018, her successor completed an unaudited actual financial report finding year-end salaries were actually $18.7 million higher than what was estimated by Michel, leading to a drop in Sweetwater's rating to BBB+ from A.

The Commission found that the related disclosures failed to reveal Sweetwater's true financial condition, that the 2018 budget projections were inconsistent with its actual expenses, and that Sweetwater's budget monitoring procedures did not consider current conditions.

These types of actions aren't novel for the Commission, as a number of other educational institutions have faced enforcement action for similar infringements, including Park View School in Arizona and California's Tri-Valley Learning Corporation in 2020.

While the SEC has not hesitated to bring actions against school districts, the Commission rarely seeks monetary penalties against municipal issuers because that penalty is ultimately borne by taxpayers who were not implicated in any wrongdoing.

Lawyers for Michel and Sweetwater failed to respond to requests for comment.

By Connor Hussey

09/16/21

BY SOURCEMEDIA

RBC Capital Markets to Pay More than US$800K to Settle U.S. SEC Charges.

TORONTO — RBC Capital Markets LLC has agreed to pay more than US$800,000 to settle U.S. Securities and Exchange Commission charges over the way municipal bond offerings were allocated.

The U.S. regulator said Friday that over a nearly four-year period that RBC improperly allocated bonds intended for institutional customers and dealers.

The SEC says the bonds went to "flippers," who then resold or "flipped" the bonds to other broker-dealers at a profit.

"We will continue to pursue those who undermine priority rules and crowd out legitimate retail or institutional customers," said LeeAnn Gaunt, head of the SEC's Public Finance Abuse Unit.

The SEC said that without admitting or denying the findings, RBC consented to a public administrative and cease-and-desist order that found it violated provisions around disclosure, fair dealing, and supervision and that it failed to supervise some of its registered representatives.

The bank on Friday said it had no comment on the case.

RBC was ordered to pay a US$150,000 penalty, disgorgement of US$552,440, plus prejudgment interest of US$160,886.

The SEC also settled charges against Kenneth Friedrich, RBC's former head of municipal sales, trading and syndication, and Jaime Durando, the head of RBC's municipal syndicate desk.

Friedrich agreed to a censure and to pay a civil penalty of US$30,000. Durando agreed to a censure and to pay a civil penalty of US$25,000.

The Canadian Press

This report by The Canadian Press was first published Sept. 17, 2021.

RBC Resolves U.S. SEC Charges Over Bond Abuses, is Fined.

Sept 17 (Reuters) – A Royal Bank of Canada (RY.TO) unit was censured and will pay more than $863,000 to resolve U.S. regulatory charges it broke rules meant to give retail and institutional investors priority in buying new municipal bonds.

In a civil settlement announced on Friday, the U.S. Securities and Exchange Commission said RBC Capital Markets LLC improperly allocated bonds to investors known as "flippers" who quickly resold their bonds to other broker-dealers at a profit.

Municipal bonds are typically issued by states, cities and school districts to fund operations and projects, and contain tax advantages over corporate and U.S. government bonds.

The SEC said RBC knew or should have known that giving priority to flippers violated its rules on bond offerings it underwrote.

It said RBC also improperly bought new bonds it had not underwritten from flippers, rather than wait in line to buy those bonds from the underwriters.

The alleged violations occurred from 2014 to 2017.

RBC's payout includes a $150,000 civil fine, plus disgorgement and interest.

Two RBC officials, head of municipal syndication Jaime Durando and former head of municipal sales Kenneth Friedrich, were also censured by the SEC and fined a combined $55,000. Friedrich left the bank in 2016.

None of the defendants admitted or denied wrongdoing. RBC closed the flippers' accounts and improved surveillance to help avert a recurrence.

RBC declined to comment. Lawyers for the other defendants did not immediately respond to requests for comment.

The SEC has reached several settlements over flipping abuses in municipal bonds, including a $10 million accord with Switzerland's UBS AG (UBSG.S) in July 2020.

Reporting by Jonathan Stempel in New York; Editing by Chizu Nomiyama and Dan Grebler

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RBC to Pay More Than $863K to Settle Charges over Muni Bond Sales.

RBC Capital Markets agreed to pay more than $863,000 to resolve charges that it circumvented procedures aimed at giving institutional and retail investors priority allocations in certain municipal bond offerings over a four-year span, the Securities and Exchange Commission announced on Friday.

From January 2014 and December 2017, RBC improperly allocated bonds to "flippers," unregistered traders who then resold the bonds to other broker-dealers at a profit. In three instances, RBC also violated the issuer's instructions to give retail investors priority and instead sold them first to flippers, the SEC said. RBC used its relationship with the flipping firms to improperly obtain bonds for its own inventory in cases where it was not the underwriter, according to the order.

"RBC did not always follow the standard methodology when it did not have priority instructions from issuers, and, in 41 instances when orders exceeded the bonds available, it failed to prioritize institutional customer and/or dealer orders ahead of flipper orders," the SEC said in the order.

The SEC charged RBC with violating the order disclosure, fair dealing, and supervisory provisions of Municipal Securities Rulemaking Board Rules and the related Exchange Act provision. The settlement includes a censure, a fine of $150,000, disgorgement of $552,440, plus prejudgment interest of $160,886.

A spokesperson for RBC declined to comment. The firm settled the charges without admitting or denying the findings, the SEC said. The agency sued the so-called flipping firms, RMR Asset Management and Core Performance Management, separately in 2018.

The SEC has pursued related violations more than half a dozen times since 2018, with one of the largest resulting in a $10 million fine against UBS Financial Services in July 2020.

In its case against RBC, it also brought charges against Kenneth G. Friedrich, RBC's former head of Municipal Sales, Trading and Syndication, and Jaime L. Durando, the head of RBC's municipal syndicate desk, who agreed to pay fines of $30,000 and $25,000, according to the SEC's press release and orders. In addition, Friedrich consented to a six-month limitation on supervisory activities and a six-month prohibition on trading negotiated new issue municipal securities, the SEC said.

The SEC found that Friedrich and Durando permitted the "improper allocation and sale of new issue bonds to the flippers," and that Friedrich also allowed for the "improper purchase of new issue bonds for RBC's own inventory through the flippers," it said in a press release.

The two agreed to cease-and-desist orders, without admitting or denying the findings, the SEC said.

Friedrich did not respond to a request for comment left on social media, and Durando did not respond to a similar request, left with the spokesperson.

"We will continue to pursue those who undermine priority rules and crowd out legitimate retail or institutional customers from getting access to newly issued municipal bonds," LeeAnn G. Gaunt, chief of the SEC's Division of Enforcement's Public Finance Abuse Unit, said in a statement.

advisorhub.com

by Miriam Rozen

September 17, 2021

SEC Fines Ex-Broker for Retail Order Period Scheme.

A former broker has agreed to be barred from the industry and pay a $40,000 penalty to settle Securities and Exchange Commission charges he dishonestly obtained new-issue bonds meant for retail customers, instead placing orders on behalf of broker-dealers.

The settled proceeding against Anthony Falsetta, announced Tuesday, is the latest in a string of SEC cases targeting violations of retail order periods. Some of that conduct has been labeled “flipping,” though that is not an official legal term, because of the practice of “flipping” the bonds to other broker-dealers at a profit. Falsetta did not admit nor deny the SEC’s findings.

“Between January 2016 and April 2018, Falsetta violated retail order period priority provisions in certain new-issue municipal bond offerings by placing orders for broker-dealers, who were attempting to buy bonds for their inventory, as retail customer orders,” the SEC found. “Falsetta did so despite knowing that pursuant to issuer priority rules, orders on behalf of broker-dealers do not qualify for retail priority.”

According to the SEC, Falsetta earned about $122,353 in commissions on 106 retail allotments he sold to Hilltop and Wells Fargo (WFC) while acting as a broker at Philadelphia-based Drexel Hamilton. As an institutional sales representative, Falsetta marketed new-issue municipal bonds that Drexel Hamilton was offering.

The SEC found that Falsetta in January 2016 contacted Daniel Tracy, a Hilltop representative who was the subject of a separate SEC action in July, and invited him to submit orders for new-issue bonds. Falsetta had previously worked together with Tracy at a different firm, and Falsetta knew the orders would be for Hilltop’s inventory, the SEC said. Falsetta had a similar arrangement with an unnamed Wells Fargo (WFC) representative, the SEC found.

“Falsetta understood that the stock orders he received from Tracy and Trader A did not qualify for retail priority,” the SEC found. “Falsetta submitted these orders as retail to create the false appearance that they were submitted on behalf of an individual rather than on behalf of a broker-dealer.”

The SEC has been worried about this and similar conduct for several years now, in part because it risks crowding legitimate retail purchasers out of offerings. In perhaps the most significant of these cases, the SEC in 2018 charged two firms and 18 individuals with operating a wide-ranging scheme to circumvent retail order restrictions.

Further cases followed, some linked to that initial case. Last year Roosevelt & Cross Inc. and its CEO agreed to pay some $1 million to settle the SEC’s charges linked to that flipping investigation.

The SEC said Falsetta took certain steps to conceal his activity, including delaying writing the sales tickets for the orders until the bonds were “free to trade.” This created the false appearance that the bonds were sold in the secondary market, the SEC alleged.

Falsetta’s conduct violated the anti-fraud provisions of the securities laws, as well as Municipal Securities Rulemaking Board rules G-17 on fair dealing and G-11 on primary offering practices.

Falsetta signed a statement attesting to his inability to pay disgorgement, though under the terms of the settlement he will pay the $40,000 civil penalty in installments. He can reapply to be eligible for a securities license after three years.

By Kyle Glazier

BY SOURCEMEDIA | 08/31/21

Which Side Are You On? Municipal Broker/Dealer Takes Both Sides.

On Aug. 26, 2021, the U.S. Securities and Exchange Commission ("SEC") instituted enforcement proceedings against Rush F. Harding III, the 65-year-old co-founder of Crews & Associates, Inc. ("Crews"), a Little Rock, Arkansas, broker/dealer and municipal advisor, and against Crews for unfair dealings in the bonds of Ohio County, West Virginia. County offices are in Wheeling, West Virginia. In 2006 the County issued $81 million of bonds bearing interest at 8.25%, and which had a make-whole provision, making calling them prohibitively expensive. In 2007 Crews began a business relationship with the County, and by 2015 had underwritten nine bond offerings for the County.

Municipal Broker
Harding, on behalf of Crews, organized two tender offers (in 2012 and 2014) to purchase the outstanding 2006 bonds, as market interest rates had fallen significantly since 2006, making an offer at a price higher than the market for the 2006 bonds, an attractive way for the County to reduce its debt service costs. The County funded the buybacks by issuing new lower interest rate bonds underwritten by Crews. Crews then purchased approximately $1 million of the 2006 bonds on the open market at 106.69% of par. It then sold those bonds to two Crews customers.

In 2015 Crews again bid on the 2006 bonds, buying $3.12 million at 107.2% of par, $2.5 million of which it sold to a Crews affiliate of which Harding was also the CEO. The County did not in any of these transactions retain a municipal advisor to represent its interests, "relying instead (per the SEC) on its relationship with, and the expertise of, Crews."

As required by Municipal Securities Rulemaking Board ("MSRB") Rule G-17, on Dec. 14, 2015, Crews sent the County a disclosure letter that documented the relationship between Crews and the County and acknowledged its obligations to deal fairly with the County. That letter asserted that it " had not identified any potential or actual material conflicts that required disclosure." Crews did not disclose that it had acquired through its affiliate $2.5 million of the 2006 bonds. Before the tender offer urged by Crews, Crews continued to purchase 2006 bonds for the affiliate.

Dealer Takes Both Sides
In December 2015, the tender offer was priced at 110% of par. When the tender closed in February 2016, the affiliate tendered 71% of the 2006 bonds tendered to the County. The SEC noted that the tender resulted in "significant savings" for the County. In connection with the tender, the SEC also found that Harding and Crews violated MSRB Rule G-27 for failing to have adequate supervisory systems. Crews made a net profit of $34,631; Harding was paid $36,524 in commissions; and the affiliate made a net profit of $27,153.

Harding and Crews consented to the entry of the SEC enforcement proceedings. As a result, Harding was censured and ordered to pay disgorgement of $36,524, as well as a civil penalty of $100,000. Crews was also censured, ordered to disgorge $44,072, and ordered to pay a civil penalty of $200,000. Ohio County and the rest of the capital markets might benefit not only from considering the way in which it and its tax-paying citizens were victims, but also from considering the frequency of abuses in the offering of municipal securities. See my Sept. 29, 2020 Blog "What if the Advice is Suspect? Municipal Securities Advisor Registration and Dereliction."

Thursday, September 2, 2021

MSRB Compares ATS And Broker's Broker Trading Platforms: Cadwalader

The Chief Economist for the MSRB analyzed the effect of electronic trading technology by comparing trading activity on alternative trading systems ("ATSs") with broker's broker platforms.

The author drew the following conclusions:

- ATS platforms (i) are more likely to include inter-dealer trades that are smaller and involve municipal securities with "complex features" (g., insured bonds and bonds with call features) and (ii) provide more robust search functions as compared to broker's broker platforms.
- ATS platforms appear to promote "visible liquidity and price discovery," particularly for municipal securities that are not commonly traded or well-known.
- Broker's broker trading platforms may be geared more towards trading for institutional investors and dealer's principal positions.

The MSRB emphasized that the analysis was "preliminary" and the results "may warrant further investigation."

31 August 2021

by Cadwalader, Wickersham & Taft LLP

NFMA Accepting Applications for At-Large Seats on the 2022-2023 Board of Governors.

We are accepting applications for At-Large seats on the 2022-2023 Board of Governors

Applications are due by October 1, 2021.

To apply, click here.

Please contact Lisa Good at lgood@nfma.org if you have questions.

Cities and States on the Frontline of Climate Change Aren't Always Upfront about Risks. Does the Municipal Bond Market Care?

Are some of our most popular regions becoming uninhabitable?

In mid-August, as water in the Colorado River dwindled, the Metropolitan Water District of Southern California declared a "water supply alert," asking its 19 million customers to voluntarily conserve water. With many California counties already in a state of drought, mandatory restrictions could be

put in place in the coming months, Governor Gavin Newsom said.

A few months earlier, officials in Miami-Dade County made a very different announcement, releasing a splashy "Sea Level Rise Strategy" that attempted to answer the question "how can we gracefully, strategically live with two feet of additional sea level rise?" But one environmentalist told the New York Times the blueprint fell short, offering "just enough to reassure developers that Miami's safe enough to build in."

Across the country, state and local governments are hustling to tackle challenges from changing climate, while simultaneously preparing for things to only get worse. It raises uncomfortable questions: at what point is Miami's waterlogged coastline just too wet? How many 100+-degree days can Phoenix, the country's fastest-growing city for the fifth-straight year, handle?

We're barely prepared for the immediate complications, forget the existential ones, public finance professionals say. Government officials often are loathe to admit the dangers their communities face. There is no standard guidance or regulation on how to document climate risk, let alone mitigate it.

More to the point, anyone looking for discipline from the $4 trillion municipal bond market, which funds state and local governments and their projects, will be disappointed.

"It's just amazing, the power of the (muni-bond) tax exemption and the avoidance of taxes. It's an unbelievable force in America," said Thomas Doe, president of Municipal Market Analytics, a Massachusetts-based provider of muni-bond market data.

"Look at the migration to Florida, Texas, and Arizona," Doe said. "You may be able to live there for a short period of time, but it's not going to be a 20-year experience." He calls it denial: "It won't happen while I'm living there." "I can't believe there will be a day when water won't come out of the tap."

Researchers at the Brookings Institution came to the same conclusion in a working paper published last September.

"In municipal finance, there appears to be almost no meaningful disclosure of climate-related risks," the researchers wrote. "Using some of the latest science projecting spatially resolved potential climate impacts, we show that there is no detectable difference in the level of municipal disclosure between communities most at risk from climate change and those least exposed to physical impacts."

"A central challenge seems to be not analysis but imagination," they add.

It's not just the thousands of ordinary Americans flocking to the "smile states" in search of sun and lower taxes — or the people buying tax-exempt bonds — who add to the risk, Doe says. The entire municipal market makes it possible for people and resources to migrate to areas that arguably may be least prepared to receive them.

Take California's Metropolitan Water. In June, the utility sold $100 million of bonds to refinance some that had been issued earlier. It has $2.6 billion in bonds outstanding, which carry the top possible rating from the two largest rating agencies, Moody's and S&P Global.

Metropolitan does note the risks posed by climate change, from flooding that puts pressure on its infrastructure to drought that may limit its supply, in its bond offering statement. But it adds, "Metropolitan is unable to predict with any certainty how climate change will ultimately affect Metropolitan or State water supplies or whether Metropolitan will be required to take additional mitigation measures."

In early August, some of the bonds maturing in 2033 traded at 140.67, well above par — the 100 price typically due at maturity — in a sign investors will are willing to pay handsomely to look past all that uncertainty for the next 12 years.

“These risks are not incorporated in the municipal market. At all,” Doe told MarketWatch. “Because investors want the tax exemption, they’re not saying ‘no’ because they want the product. They don’t discern risk. It’s not a prioritized risk in the ratings. So the rating agencies aren’t penalizing the issuer, no-one is telling the issuer you have to disclose risks. No-one wants their cost of capital to go up.”

Ratings

The Brookings paper takes aim at the bond raters. While acknowledging that credit firms cannot fully disclose their methodology, the researchers still found what they call big gaps.

Among other things, they note, when Moody’s, S&P and Fitch address climate risk, it tends to be backward-looking, rather than proactive. The paper highlighted a 2017 Moody’s downgrade of Puerto Rico bonds, as an example: “Hurricane Maria hits in September 2017; the next month Moody’s downgrades the (Puerto Rico) revenue bond out of revenue concerns but still makes no mention of climate change affecting the probability of Maria-like events in the future.”

“I understand that particular criticism,” said Marcy Block, senior director of sustainable finance for Fitch. (Moody’s did not respond to a request for comment.)

Fitch does include a climate risk component (called an “ESG relevance score”) in all of its ratings, Block said, and some issuers — in the Florida Keys, for example — are graded as higher-risk because of capital needs relating to flooding and other environmental impacts.

“(S&P Public Finance) specifically incorporates an ESG paragraph into our issuer-level credit rating reports and research to provide transparency on how ESG factors may affect a particular entity’s credit profile,” the credit firm said in emailed remarks. It also discloses if one of its steps was driven by an ESG (environmental, social or governance) factor, the group said.

“There’s a recognition that there’s still more that can be done,” Fitch’s Block said. “I think it’s clear that the disclosure so far from issuers has been very weak. Whether that’s driven by investors continuing to demand more information or regulatory change, I think you’ll see more and more disclosure coming forward.”

Regulators

Many market participants are hoping for more clarity and enforcement from regulators. In March, the U.S. Securities and Exchange Commission announced an evaluation of climate-change disclosures. The SEC and federal prosecutors have since opened probes into whether a subsidiary of Deutsche Bank overstated its use of sustainable investing criteria, according to a Wall Street Journal report, citing people familiar with the matter.

Enforcement efforts might go only so far. The SEC might look to extract fines from fund managers who make misleading ESG claims or it might go after issuers who knowingly obscure risks. But its role isn’t to set standards that will force issuers to identify their risks, disclose them, and get rated on them.

Mark Kim is CEO of the Municipal Securities Rulemaking Board (MSRB), which sets rules around trading and transacting in the muni market but, like the SEC, does not have the ability to set issuer standards. In an interview with MarketWatch, Kim said, “There’s certainly more work to be done. I

think the market's understanding of climate risk is evolving. Today, reasonable investors consider climate risk to be material."

Ideally, all disclosure would be standardized, not just a reflection of whatever quirks belong to particular issuers, Kim noted, so "investors can compare apples to apples."

Asked whether Congress should amend its charter so the MSRB could make disclosure rules, Kim said, "That's a really important policy question. We will leave it to Congress to decide."

Investors

"We recognize that climate risk is a real threat, it's not just some secular theme that's 10, 20 years out. It's here now," said Sean McCarthy, head of the municipal credit research team for $2.2 trillion money manager PIMCO.

"I think disclosure is the area where people want to see more," McCarthy told MarketWatch. "It's getting better, but it's a risk factor that needs to be discussed. Large borrowers, bellwether borrowers, like the state of California, are pretty good at it. Where it could be better is on the local government level but, there's a cost associated with. I think states could help out a little bit more."

McCarthy also thinks industry-wide standards would be ideal, but like any institutional investor, his team will still do its own credit analysis, he said.

He offered one example: PIMCO rates single-site project bonds in coastal areas lower and demands a slightly higher yield as compensation for taking on additional risk. And he noted that the municipal market broadly agrees, paying less for such bonds than it does for similar inland deals — but only by about 5 basis points.

As previously reported, demand for municipal bonds has run so hot in recent months that it's pushed yields to all-time lows (yields move in the opposite direction as prices) and inflows to mutual and exchange-traded funds have smashed weekly records multiple times in 2021.

MMA's Doe notes a muni-market irony: some of the country's climate-change hot spots, like California and Florida, are also some of the wealthiest, where demand for tax-exempt investments is highest. He believes the municipal tax exemption is one of the biggest reasons the market looks the other way, rather than confronting climate risk.

Issuers

To be sure, plenty of people think the worst-case scenarios people dream up are simply too pessimistic. For example, McCarthy calls the question of out-migration from some of the country's most popular areas "generational."

"I am worried about population trends," he said, but views tax policy as an immediate catalyst of migration trends.

Some municipal officials argue they're far more prepared than the market may realize. Mark Hartman, a Canadian who moved to Phoenix several years to take a role as that city's chief sustainability officer, points out that his adopted hometown has always been a desert, adapting to heat long before anyone worried about manmade climate change.

"People here, it's in their DNA," Hartman told MarketWatch. "Just like the trees here are desert-adapted. We look at innovative projects and policies that will help cool our city."

In a study conducted by Arizona State University, which makes Phoenix a sort of climate-change

living laboratory, two city neighborhoods just two miles apart were found to have a temperature difference as high as 13 degrees, pointing to the efficacy of climate mitigation efforts like planting trees, “cool pavement” technology, and more, Hartman said.

But the tricky thing about climate change is that it represents, well, change — not necessarily the same challenges communities faced in the past.

“The latest science about climate change shows the system changing rapidly, with synergistic impacts that will have substantial and growing impacts on physical assets and public welfare, including the economic viability of communities on the front lines,” the Brookings researchers wrote.

“Extensions of the latest climate science suggests that plausible tail risks are even larger and more immediate. The problem of disclosure reflects a problem of imagination.”

Doe likes to talk about climate risk in three stages: denial, which he thinks we’ve largely moved beyond, defense, and departure.

We are now in the “defend mode,” he said. “There will be rationales made as to why an investment should be made to preserve a community. We’ll build gates or drains to protect us. We’ll establish resilience committees. But will it be sufficient? Does anyone have the timing right? And then, is that the best use of the money?”

No family likes to prepare for death, but eventually most of us write wills, he said. Similarly, “no-one wants to say a place is going to become uninhabitable.”

MarketWatch

By Andrea Riquier

Aug. 28, 2021

Characteristics of Municipal Securities Trading on Alternative Trading Systems and Broker’s Broker Platforms.

Did you know market share of alternative trading systems (ATS) and broker’s broker platforms makes up 58% of inter-dealer trades?

MSRB Chief Economist Simon Wu tracks how electronic muni trading on such platforms affects the market in his latest paper.

Underwriter Settles SEC Charges for Failing to Disclose Conflicts: Cadwalader

An Arkansas-based broker-dealer and its former CEO settled SEC charges for fair dealing violations arising from a municipal bond tender offer.

In separate orders, the SEC found that, at the instruction of the former CEO, the broker-dealer recommended to a West Virginia county that it (i) effect a tender offer for bonds issued in 2006 in order to decrease its outstanding debt service expense, (ii) offer to purchase the outstanding bonds

from the bondholders and (iii) bankroll the purchase of the bonds by selling new bonds with a lower interest rate that the broker-dealer would underwrite. According to the SEC's findings, the broker-dealer and its former CEO failed to disclose to the county when making those recommendations that it and its affiliates had recently purchased and sold a significant amount of the bonds that were the subject of the tender offer, which bonds were then sold back to the county at a significant profit.

As a result of its findings, the SEC determined that (i) the broker-dealer and its former CEO violated MSRB Rules G-17 ("Conduct of Municipal Securities and Municipal Advisory Activities") and G-27 (" Supervision") and (ii) the former CEO caused the broker-dealer to violate Section 15B(c)(1) ("Discipline of municipal securities dealers; censure; suspension or revocation of registration; other sanctions; investigations") of the Exchange Act.

To settle the charges, the broker-dealer and former CEO each agreed to (i) a censure, (ii) cease and desist from future violations, (iii) pay $44,072 and $46,481 in disgorgement and prejudgment interest, respectively, and (iv) pay $200,000 and $100,000 in civil money penalties, respectively. In addition, the former CEO agreed to "certain undertakings and limitations on activities."

Cadwalader Wickersham & Taft LLP

August 26 2021

Legislative Path Forward for Key Muni Legislation.

Yesterday, the House advanced the $3.5 trillion budget reconciliation framework, a legislative vehicle to be used for additional infrastructure spending after weeks of back-and-forth between a small caucus of Democratic moderates and House Leadership. The group pushed for a vote on the Senate bipartisan infrastructure package before advancing the budget framework, however, conceded, pushing the vote to September 27th setting up what will likely be a legislative battle through the fall.

With multiple infrastructure packages moving through Congress in the coming months, below is a primer on the status of key municipal bond legislation and prospects for each spending package:

Bipartisan Infrastructure Package

Earlier this month, the Senate passed a $1 trillion infrastructure spending package that includes nearly $600 billion in new funding. While a new direct-pay bond was originally included in the Senate outline, the American Infrastructure Bond was removed from the package due to a lack of offsets and the inability to reach a consensus on reimbursement rates. **While light on key municipal provisions, the bill relies heavily on the usage of PABs, including:**

- **The package would allow states to issue PABs to finance broadband deployment, specifically for projects in rural areas where a majority of households do not have access to broadband;**
- **Permit carbon capture and direct air capture (DAC) technologies to be eligible for PAB financing. These bonds would be 75 % exempt from the volume cap;**
- **The bill increases the current cap of tax-exempt highway or surface freight transfer facility bonds from $15 billion to $30 billion as proposed by the bipartisan BUILD Act (S.881). Currently, $14,989,529,000 billion of the $15 billion cap has been issued or allocated.**

As part of the House negotiations this week, the legislation will be brought to the House floor by September 27th, and will almost certainly become law shortly thereafter setting the stage for the budget reconciliation package that will include additional infrastructure spending, possibly including munis, following through on the Biden Build Back Better Agenda.

Infrastructure Focused Budget Reconciliation

Following the passage of the bipartisan package, the Senate turned its attention to the next phase of infrastructure spending, a robust budget reconciliation outline that provides the ability for an additional $3.5 trillion of federal spending. While initial policy details are light by design, through discussions with key Hill and Administration staff, the MBFA and BDA believe that municipals with receive consideration in the tax title of this potential package, with House Ways and Means Chairman Richie Neal (D-MA) a key ally for the municipal bond industry, helping to guide the path.

We remain focused on the municipal provisions included in the LIFT Act which was introduced earlier this year by House Ways and Means Member Terri Sewell (D-AL). This package includes:

- **The reinstatement of tax-exempt advance refundings,**
- **Raise the BQ debt limit, and**
- **Creation of a new direct-pay bond exempt from sequestration.**

While we believe municipals will play a role in this package, the road towards passage will likely be narrow. Senate and House moderates have pushed back at the $3.5 trillion price tag, so we expect that to come down substantially for passage. We remain focused on the LIFT Act provisions as they have support in both Chambers and remain a common-sense infrastructure solution at a low cost to the Federal government.

The MBFA and BDA will continue to provide updates as they become available.

Bond Dealers of America

August 25, 2021

SEC Fines Firm and Ex-CEO for Failing to Disclose Conflict of Interest.

Arkansas-based Crews & Associates has agreed to pay more than $200,000 and its former CEO more than $100,000 to settle Securities and Exchange Commission charges they violated fair dealing and supervision rules by failing to disclose the firm’s relationship with an affiliate that profited from business the firm did with a West Virginia county.

The SEC announced the settled administrative proceedings against the firm and former CEO Rush Harding III Thursday, a significant enforcement action that is only the third muni case of 2021 following a busy 2020 for the Public Finance Abuse Unit.

The charges stem from Crews? October 2015 recommendation that Ohio County, West Virginia, reduce its debt burden through a tender offer for bonds it had issued in 2006.

The SEC said that following the discussions of the tender offer, Crews, with Harding’s approval, purchased millions of dollars of the county’s outstanding bonds and sold them to an entity affiliated

with Crews and to Crews' customers. Almost all of the bonds Crews acquired were eventually sold to its affiliate and tendered back to the county at a price that Crews had recommended, resulting in a net profit to the affiliate.

"In municipal bond offerings, underwriters must fully disclose to issuers their financial interests in the deal," said LeeAnn G. Gaunt, chief of the Enforcement Division's Public Finance Abuse Unit. "Failure to do so is a violation of their obligation to deal fairly with issuers."

Both Crews and Harding agreed to the settlements without either admitting or denying the SEC's findings.

The 2006 bonds, maturing in 2035 and bearing interest at 8.25%, contained a make-whole call provision that rendered calling them cost-prohibitive, and an ordinary refunding or advance refunding impractical, the SEC said. Crews had a business relationship with the county since 2007, and had underwritten nine bond offerings for it.

According to the SEC, Crews recommended that the county offer to pay bondholders a price higher than the current market price of its outstanding bonds to incentivize bondholders to tender their bonds. Crews also recommended that the county fund its purchase of those previously issued bonds through the sale of new, lower interest rate bonds, which Crews would underwrite. When Crews made these recommendations, the SEC found, the firm did not disclose to the county that Crews had recently acquired more than $1 million of the county?s outstanding bonds at market prices and then sold them to two customers.

In the months following the initial discussions of the tender offer, the SEC alleged, as Crews and the county finalized the terms of the proposed transaction, Crews purchased some $4.8 million more of the county's outstanding bonds at market prices and sold them to an affiliated entity and to Crews' customers. Almost all of the bonds Crews acquired were eventually sold to the affiliate and tendered back to the county by the affiliate at a price that Crews had recommended. Crews did not disclose to the county that the affiliate had acquired bonds to be tendered, or the resulting conflict of interest created by the affiliate's financial interest in the tender offer, the SEC said.

The county authorized the issuance of $10 million of new municipal bonds to fund its purchase of the 2006 bonds. In January 2016, the notice of tender was publicly posted, with the maximum acceptable price set at 110% of par.

Crews then continued to buy 2006 bonds from third parties and from Crews customers at market prices, in some cases mark them up, and selling them to the affiliate, the SEC said.

By the time of the tender date, Crews had purchased $5.9 million in principal value of the bonds on behalf of its affiliate. On the tender date of Feb. 16, 2016, the affiliate offered to tender all of these bonds to the county's tender agent at the maximum acceptable price. Since the county did not receive a sufficient number of tender offers at prices lower than the maximum acceptable price, the county accepted the offer of the affiliate.

In all, the SEC found, the affiliate tendered 71% of all 2006 bonds that were tendered to the county. The deal did save the county money, the SEC found.

But as a result of the markups it charged on its transactions with its customers and the affiliate, Crews made a net profit of $34,631. The affiliate made a net profit of $27,153 as a result of its purchases of the bonds from Crews and its tender of those same bonds to the county.

MSRB Rule G-17 requires broker-dealers to deal fairly with all market participants, which the SEC

said the firm violated by failing to make the county aware of the secondary market transactions going on. MSRB Rule G-27 requires that firms have in place a supervisory system reasonably designed to ensure compliance with all applicable securities laws and rules, but the SEC found that Crews' system provided no means of accountability and so the transactions were not reviewed as they should have been.

By violating these rules, the SEC found, Crews violated Section 15B(c)(1) of the Securities Exchange Act, which prohibits dealers from using the mail or "any means or instrumentality of interstate commerce" to execute municipal securities transactions in violation of any MSRB rule.

Crews agreed to pay a civil penalty of $200,000 and disgorgement of $34,631 and prejudgment interest of $9,441. The SEC said Crews has already taken steps to correct the supervisory problems that led to the action.

"Crews and Associates is pleased to resolve this matter and is now looking to the future," said Paul Maco, a Bracewell attorney who represented the firm. Maco said the firm is devoting its full attention to serving its customers and growing its business.

Harding agreed to pay a $100,000 penalty and disgorgement of $36,524 and prejudgment interest of $9,957. Harding, who is still a registered broker, may not participate in new issues or tender offers for 12 months. An attorney for Harding did not respond to a request for comment.

By Kyle Glazier

BY SOURCEMEDIA | MUNICIPAL | 08/26/21 12:45 PM EDT

August Issue of GFOA's Government Finance Review.

This month's issue of *Government Finance Review* puts a spotlight on state banks. Are state banks a useful economic development tool with future promise?

Other topics from the magazine include budgeting bias, strengthening risk management, a spotlight on GFOA scholarship recipients, and more.

Financial Accounting Foundation Trustees Announce Appointment of New Chair of the Governmental Accounting Standards Advisory Council (GASAC)

Norwalk, CT—August 24, 2021 — The Board of Trustees of the Financial Accounting Foundation (FAF) announced today the appointment of Elizabeth (Beth) Pearce as Chair of the Governmental Accounting Standards Advisory Council (GASAC). Ms. Pearce's term will begin January 1, 2022.

Ms. Pearce currently serves as the Treasurer for the State of Vermont. She is the state's banker and investment officer. In her role, she manages short and long-term debt, the administration of three retirement systems, unclaimed property funds, and plays an advisory role to state policy makers.

The GASAC advises the Governmental Accounting Standards Board (GASB) on strategic and technical issues, project priorities, and other matters that affect standard setting. The GASAC

provides the GASB with diverse perspectives from individuals with varied governmental, professional, and occupational backgrounds.

The FAF Board of Trustees appointed Ms. Pearce as a member of the GASAC, nominated by the National Association of State Treasurers, beginning January 1, 2021. She will succeed Mr. Robert W. Scott, who joined the GASAC in 2011 and became Chair in 2015.

“It is a pleasure to welcome Beth Pearce as our new GASAC Chair. She will play an important role in the GASB process,” said Kathleen L. Casey, Chair of the FAF Board of Trustees. “We would also like to thank our departing Chair, Robert Scott, for his time, expertise, and the contributions he made to the standard-setting process,” she added.

For a complete list of current Council members, visit the GASAC webpage.

Treasury Guidance on Non-Entitlement Units is Now Available.

The United States Treasury has issued guidance on non-entitlement units (NEUs) providing additional information on eligibility and a step-by-step guide for states to allocate and distribute funds to their NEUs. States should follow the guidance and calculate allocations based on the list of local governments and their respective populations. The statute requires that all allocations to eligible governments be based on population. Treasury expects to make payments to states for distribution to NEUs in two equal tranches approximately twelve months apart.

NASACT

MSRB Offers Remote Municipal Advisor Principal Exam.

The MSRB will allow individuals seeking to qualify as municipal advisor principals to take the Municipal Advisor Representative Qualification Examination (the “Series 54 Exam”) online. The accommodation is temporary and intended to address persistent COVID-19 challenges.

To schedule an online test, individuals must submit an interim accommodation request form to FINRA. Once this is processed by FINRA, individuals may schedule a test appointment online. Information on the sign-up process and exam will be published during the week of August 15, 2021, on a dedicated webpage on MSRB.org.

The MSRB will also seek to extend the relief under Supplementary Material .09 (“Temporary Relief for Municipal Advisor Principal”) to MSRB Rule G-3 (“Professional Qualification Requirements”) from the current compliance date of November 12, 2021.

Cadwalader, Wickersham & Taft LLP

13 August 2021

What Will the End of LIBOR Mean for the Multifamily Industry?

Learn what's happening with the switch to a new loan index.

The multifamily housing industry is moving closer to phasing out its long-standing index for adjustable-rate loans and other financial transactions.

The London Interbank Offered Rate (LIBOR), which covers five currencies and seven tenors, is on its way out after years of being a globally accepted benchmark. The Alternative Reference Rates Committee (ARRC), a group of private-market participants convened by the Federal Reserve and the New York Fed, has identified the Secured Overnight Financing Rate (SOFR) as LIBOR's replacement.

LIBOR was supposed to be retired by the end of this year, but that date has been extended to June 30, 2023, for most U.S. LIBOR values. The one-week and two-month LIBOR will still expire at the end of 2021.

"In commercial real estate, floating interest rates are commonly indexed off LIBOR," says Steven Fayne, principal at Align Finance Partners. "However, its uses span far more than just mortgages. Corporate loans, government bonds, credit cards, swaps, and myriad other financial products currently use LIBOR as a benchmark."

Citi Community Capital (CCC), a leading provider of financing for affordable housing, uses one-month LIBOR swap rates for floating-rate construction loans and other community development floating-rate loans. In addition, CCC uses LIBOR swap rates to establish fixed rates for permanent period fixed-rate loans, according to Barry Krinsky, national production manager.

Despite LIBOR's widespread use and long history, U.S. financial regulators have been pushing for the change to SOFR because it is believed to be a better and more resilient rate. One reason for this is the sample size for calculating LIBOR has been declining since the Great Recession. There's now less than $1 billion a day in transaction volume compared with $1 trillion a day for SOFR, says Blake Lanford, managing director in the trading department at Walker & Dunlop.

Other key differences are also driving the move. LIBOR is an average of interest rates reported by major banks, and some have been accused of misrepresenting their numbers to achieve better returns. SOFR, a broad measure of the borrowing of cash overnight collateralized by Treasury securities, is based on actual transactions rather than a survey.

"LIBOR is forward-looking, so the one- and three-month LIBOR is an expectation of where it would be one or three months in advance based on a forward curve," says Lanford. "SOFR is currently backward-looking, using a 30-day average."

What's Happening in Multifamily

Fannie Mae and Freddie Mac moved over to using SOFR for their variable-rate loans last September.

"There were a few months when there was some optionality, but they wouldn't accept anything after December that was LIBOR-based," says Lanford.

"Everything now from Fannie and Freddie is SOFR-based on new loans."

CCC also is planning on ceasing the use of LIBOR for new loans and issuing SOFR loans in the coming months, according to Krinsky.

The firm has chosen the new index, he says, “in part because the SOFR benchmark when combined with the lending spread is expected to result in our multifamily borrowers achieving all-in borrowing rates similar to what they achieved with the LIBOR benchmark.”

In the affordable housing world, the use of LIBOR is somewhat limited. Adjustable-rate loans are uncommon in low-income housing tax credit deals because housing credit investors do not want the variable-rate exposure.

However, these loans are seen in some Section 8 transactions and during the construction phase of some affordable housing deals. Adjustable-rate loans are also seen in conventional multifamily property loans.

For the overall multifamily industry, the big unknowns are how and when will lenders transition the loans in their portfolio that use LIBOR. They’re going to have to move over to SOFR at some point.

When that transition happens there’s going to have to be a spread added to minimize any value transfer from the rate changing in favor of the investor, or borrower, says Lanford.

The good news is that many existing contracts will expire before LIBOR is phased out in mid-2023, so the parties won’t have to alter the pricing methodology currently used, according to Fayne.

“For contracts that use LIBOR as a benchmark and expire after 2023, the reference rate will need to change,” he says. “However, it’s highly likely that those contracts include ‘fallback language’ prescribing how the loan will be priced in the event LIBOR rates are no longer available.”

The next big action is expected to take place this month. “The big banks are being asked to switch over to SOFR at least on the interdealer interest-rate swaps by July 26,” says Lanford. “Once that happens, there’s going to be more progress.”

This step will cause trading activity among swap dealers on these platforms, which account for a substantially large share of trading in the interest rate swap markets, to switch from LIBOR to SOFR.

That’s going to create a more robust market, and that will be necessary to build a forward-term rate like there is for LIBOR. “We have a one-month and a three-month LIBOR,” Lanford says. “They’re trying to develop the same thing for SOFR. Right now, there’s plenty of transactions on the front end, but not as much as on longer-term futures and swaps contracts. The switch on July 26 will change that.”

Looking ahead, it’s important for developers to know what their variable-rate exposure is. “There may be some borrowers that have a schedule of real estate that’s 100% fixed rate, and they don’t have much to worry about,” he says. “For those who have some variable-rate exposure, planning in advance and matching up their loans along with any other derivatives is going to be a priority. Unfortunately, there’s not much that we know yet as far as timing, but try to anticipate that switch.”

Walker & Dunlop will provide lots of notice to the loans in its portfolio, and Fannie and Freddie will work to give as much lead time as possible as well, according to Lanford.

With representatives of the Federal Reserve and ARRC saying that SOFR should be used, developers should be cautious about loans that use a different benchmark. “I think the recommendation will soon be to think hard before using LIBOR or alternative indexes other than SOFR,” Lanford says.

Affordable Housing Finance

By Donna Kimura

July 12, 2021

Public Pension Looters Need Not Fear FBI And Law Enforcement.

The FBI's investigation into alleged false investment performance at the $67 billion Pennsylvania Public School Employees' Retirement System may suggest law enforcement is finally focused upon public pension shenanigans. That's not likely.

If you want to understand how pension looters and high-level investment scammers frequently escape prosecution, begin with studying the legal and regulatory structure of the money management industry. Successful scammers know: (1) which laws or regulations they can skirt, or break; (2) who, i.e., which agencies may come after them for their bad behavior; and (3) the limitations of different regulators and law enforcement.

A "security" is a broad term that includes many types of investments, such as municipal bonds, corporate stock and bonds, bank notes, investment contracts and more. Securities fraud occurs when someone involved with one of these investments lies, cheats, or steals in an attempt to gain a financial advantage.

Continue reading.

Forbes

by Edward Siedle

Aug 16, 2021

The Conclusion of a Long Running Pay-to-Play Case.

Many of the cases brought recently by the Commission have been either offering fraud or microcap issuer cases with the latter often centered on pump-and-dump manipulations. These cases typically fleece unsuspecting investors who purchase what appear to be inexpensive securities based on some type of guaranteed return or assurance against lost in the case of offering fraud actions or the lure of quick profits from an about to increase stock in the case of the manipulations. The outcome in all of these cases is the same – the investors lose their hard earned savings.

Some cases follow a different pattern. For example, some cases involve public officials taking a bribe in return for steering business to others. In those cases the pattern is different but for investors it is the same, they lose although it may not be as apparent. Once such case is *SEC v. Webb*, Civil Action No. 17-8685 (N.D. Ill.), a pay-to-play case.

Defendant David Webb is the mayor of the City of Markham, Illinois. In connection with a 2012 municipal bond offering designed to fund city capital projects, Mr. Webb engaged in a pay-to-play scheme. The mayor approached a contractor involved in the city capital projects and solicited a bribe. In return Mr. Webb agreed to steer a multi-million construction project to the contractor. The project would be funded from the offering proceeds of the municipal bond offering.

The complaint alleges violations of Securities Act Section 17(a) and Exchange Act Section 10(b). To resolve the action Mr. Webb consented to the entry of a permanent injunction based on the Sections cited in the complaint in late 2017. This week the Court entered the final judgment after determining monetary remedies. The Court entered permanent injunctions based on the Sections cited in the complaint. The mayor was also barred from participating in further municipal bond offerings. In addition, Mr. Webb was directed to pay disgorgement of $85,000 and prejudgment interest of $32,849.35. Those amounts were deemed satisfied by the restitution order entered in the parallel criminal case. *See* Lit. Rel. No. 25160 (August 9, 2021).

SEC Actions – Thomas O Gorman

August 12 2021

Transaction Costs During the Covid-19 Crisis: MSRB White Paper

MSRB publishes new research paper analyzing the evolution of transaction costs in the municipal and corporate bond markets during the COVID-19 liquidity crisis and the subsequent recovery.

Read the paper.

MSRB Proposes Amendments to Annual Customer Notification Requirements.

The MSRB proposed amendments to narrow the scope of the annual customer notification requirements under MSRB rules on delivery of investor brochures and transactions with sophisticated municipal market professionals.

The MSRB filed with the SEC amendments that would narrow the scope of the annual customer notification requirements under MSRB Rule G-10 (“Delivery of Investor Brochure”). The amendments would limit the persons dealers would have to notify to only those who either (i) have effected municipal securities transactions or (ii) hold a municipal securities position.

The proposal also includes amendments to MSRB Rule G-48 (“Transactions with Sophisticated Municipal Market Professionals”) that would except dealers from making such annual notifications to sophisticated municipal market professionals, so long as the required information is available on the dealer’s website.

Comments on the proposal must be submitted within 21 days of its publication in the Federal Register.

Cadwalader Wickersham & Taft LLP

August 3 2021

S&P: USPF Enterprise Sectors Treatment Of Operating Leases Under FASB's

ASU 2016-02 (ASC 842)

Background

S&P Global Ratings is updating the market with its views on the Financial Accounting Standard Board's (FASB) new standard, Leases (ASC-842), and its impact on audited financial statements of rated entities in the not-for-profit health care, higher education, charter schools, and public power and electric cooperative sectors, which S&P Global Ratings collectively refers to as enterprise sectors. With the standard now in effect for a greater number of rated entities that report under FASB standards, we are providing additional information on the treatment of operating leases under our enterprise sectors criteria. We had published an FAQ, "How New Accounting Rules Will Affect U.S. Enterprise Sectors," on March 11, 2019, on RatingsDirect and this update supersedes that commentary.

We will continue to review our approach to incorporating lease liabilities into our analysis of enterprise sectors pursuant to our criteria, particularly as governmental issuers in the enterprise sectors implement lease updates through the Governmental Accounting Standards Board (GASB) Statement No. 87-Leases after a substantial delay in the required implementation date (see last section, titled "How will GASB No. 87 impact our analytical approach to leases?") to fiscal years beginning after June 30, 2021. Since GASB No. 87 changes how leases are classified, effectively no longer recognizing the operating lease distinction, we will expect to maintain consistency and comparability across the two accounting standards, to the extent possible given nuances associated with each standard, as the enterprise sectors have entities that present financial statements under both FASB and GASB standards.

Not all of our rated FASB entities have incorporated the new lease standard, yet. In response to concerns of the impact that the Coronavirus (COVID-19) pandemic could have on stakeholders, the FASB released ASU 2020-05 in June 2020, which delayed the effective implementation dates for ASC 842 for certain public not-for-profit entities which had not yet issued financial statements reflecting adoption of the standard, which includes obligors that use conduit issuers, and all other not-fo--profit entities. Early adoption continues to be permitted. While a number of entities we rate have adopted the standard, certain entities have not yet adopted the standard due to FASB's delay of the effective implementation date.

Frequently Asked Questions

Will the lease accounting requirements result in rating changes?
Lease accounting requirements enhance transparency and add to robustness of disclosures, but are generally not expected to result in rating changes, nor have they in the past for rated entities that have adopted the standard. While the financial statement presentation under ASC 842 provides more clarity on the actual value of the lease liability, the actual lease obligations incurred by rated entities largely have remained unchanged; therefore, the accounting standards update has not been viewed as a new credit factor. We believe the financial effect of existing operating leases has been incorporated into our credit ratings and related analyses prior to the ASC 842 update.

How do we incorporate lease usage into our analysis of enterprise sector obligors?
We will assess lease usage by the following measures:

Health care. Operating lease liabilities are typically not included in our calculation of long-term debt and related ratios, and we continue to believe that our lease-adjusted maximum annual debt service (MADS) coverage metric appropriately captures lease utilization within our assessment of the financial profile. Further, as per our criteria, we retain the flexibility to make an analytical

judgment as to whether a negative consideration is warranted for the entities where liabilities or off-balance-sheet financings, including operating leases, materially bring added risk to the financial profile when not fully captured in debt to capitalization or other financial metrics. While we recognize that in certain cases the audited presentation of operating lease expense may now encompass additional expenses, such as variable lease costs, in most instances we are able to adjust for this such that operating lease expense remains comparable with prior periods, which typically consisted solely of operating and short-term lease costs. To date, there have been no rating changes driven by the change in accounting for operating leases among rated not-for-profit health care entities that have adopted ASC 842.

Higher education. While our criteria treats capital leases as debt, we have not generally treated operating leases as debt and have not included them in our MADS burden or total debt ratios. However, we review an institution's operating leases and in cases where we deem those operating leases significant compared with debt, we have assessed them in some capacity (e.g., either by including them in the MADS burden or in total debt calculations). Pursuant to our criteria, we reserve the right to adjust aspects of the financial profile assessment in order to adequately capture the risk associated with elevated operating lease usage. Since implementation of FASB ASC 842 (applicable to private colleges and universities, independent schools and some public universities that elect to follow FASB accounting standards), none of our ratio definitions and their applications have changed and, related to this matter alone, there have not been any changes in our opinion of an institution's underlying creditworthiness.

Charter schools. Pursuant to our criteria, operating lease liabilities are typically not included in our calculation of long-term debt and related ratios. However, for charter schools, we have consistently incorporated the use of operating leases into our rating analysis through our use of lease-adjusted MADS when calculating key financial ratios, such as debt service coverage (DSC) and debt burden. For example, we calculate lease-adjusted MADS coverage as earnings before interest, depreciation, and amortization plus facility lease expense/MADS plus facility lease expense. Lease-adjusted MADS coverage is generally the heaviest weighted component of our financial profile assessment for rating charter school bonds. We reserve the right to adjust aspects of the financial profile assessment when we deem the lease-adjusted MADS coverage and debt burden to insufficiently capture the risk associated with elevated lease usage.

We will continue to analyze the effect of implementation on all entities that use operating leases and update our view of the underlying creditworthiness accordingly.

Public power and electric cooperatives. Our long-standing practice has been to treat lease agreements as having debt-like attributes irrespective of whether accounting standards dictate classifying power purchase agreements as finance or operating leases. We reflect these adjustments in our fixed-charge coverage calculations, which we perform in addition to our DSC calculations. Our fixed-charge coverage focuses on payments utilities make to utility suppliers to reserve generation capacity and to their retail customers. Because we are already capturing the dominant lease and lease-like payments in our fixed-charge coverage, we believe that the changes in accounting standards do not affect coverage ratio analysis for public power and electric cooperative utilities.

When do we consider operating lease usage to be significant and compel additional adjustments to our standard ratios?

The analytic decision to make an additional adjustment within the financial profile assessment of an obligor could reflect various lease factors such as our view of the magnitude of the operating lease liability relative to the capital structure, structural elements of the leases, and the perceived strategic risk of the leasing strategy. In those instances where we believe these lease factors are not

fully captured in our ratios, we reserve the flexibility in our criteria to apply a negative adjustment in the financial profile section of the criteria. While rare, there have been instances where we have applied a negative adjustment within the financial profile section of our criteria.

How do we expect accounting for leases to differ under FASB ASC 842 compared with GASB No. 87?

Based on our initial understanding of GASB No. 87, we expect that after its implementation, most lease arrangements previously classified as operating or capital leases, will be considered finance leases, which we typically include in long-term debt. Therefore, we believe this difference in lease accounting reporting requirements under GASB compared with FASB complicates the ability to separate lease liabilities from long-term debt. However, the underlying economics of lease arrangements are unchanged solely due to the new accounting standard, so we generally do not anticipate rating changes associated with the GASB No. 87 standard. We will review whether the presentation of GASB No. 87 requires us to revisit the details of how we incorporate operating leases into our criteria–specifically as it relates to debt and coverage-related ratios.

How will GASB No. 87 affect our analytical approach to leases?

We expect to maintain analytical consistency in our approach to evaluating lease obligations and to maintain comparability across rated entities within sectors regardless of whether the rated entities follow GASB or FASB accounting standards, to the extent possible given the incongruity of the two accounting pronouncements. While early adoption is permitted, to date, S&P Global Ratings has not seen the specifics of how GASB No. 87–applicable to most public colleges and universities, community colleges, hospital districts, public transportation, public housing, local governments, and public power entities–will present on financial statements.

More broadly, since the GASB update on leases will affect all USPF credits, we will update the market on our views regarding leases beyond the enterprise sectors, including all government entities in USPF.

This report does not constitute a rating action.

30 Jul, 2021

The Use Of A Crisis To Create Opportunity In The Muni Market.

The Coronavirus pandemic has led to death, tragedies and social and economic disruptions. Most of the disruption was unavoidable and unknowable and some individuals actually saw opportunities to create services and products that would be welcomed in this environment. Others, however, saw opportunities to use the economic disruption to achieve gains by playing on the publics' fear. The municipal bond market is highly vulnerable to fear based abuse because of its mediocre performance in public disclosure and a weak secondary market.

While the municipal market is no stranger to abusive practices in bond issuance and secondary market pricing, its greatest vulnerability is in its failure to police ongoing disclosure compliance. The

Municipal Securities Rulemaking Board, or MSRB, has been given the responsibility for overseeing disclosure practices, but has little enforcement power or staff to maintain order in this massive and unregulated market. The SEC can step in to curb abuse since they do have a broader mandate, but they appear to have priorities elsewhere.

My concern today is that large investors in existing issues are using their ability to manage the information flow about a specific project to discourage smaller investors and motivate them to sell their bonds which they can then buy up at below their true value. Remember that the municipal secondary market is not a truly competitive market and even less so when the required public information filings are not being made. Their motivation for this are as diverse as:

- A need to restructure the bonds. Buying up other holders' bonds reduces their haircut on their holdings.
- Seeing the need to provide additional funding to the project which would benefit others as well.
- Seeing a high coupon long maturity bond issue which can be re-purposed for a more viable project.
- An opportunity to profit from investors fearing the worst as they tend to do when the information flow is not there.

So how does one hold back on the information flow and create an information vacuum:

- Own or gain control of 25% or more of the bonds. Trustee's, who are the main enforcers of the disclosure and payment requirements love to obtain guidance from such a proportion of bondholders in order to avoid being liable for anything they do or fail to do.
- Stop interest payments and maturity redemptions even if there are reserve funds available. This is usually justified as being done to preserve funds for legal actions or other contingencies.
- Reach a standstill agreement with the project owner whereby he too comes under the control of the majority bondholders who can then manage his information flow and other actions.
- Stop public reporting of the projects status and keep bondholders informed by teleconference where there is no written record of what was said.
- Minimize the information any non-current bondholder can see in order to make a competing price offer.
- Let the brokerage firms, who make a market in specific bonds, know you are a buyer and at what price.

You would think that the bond trustee would exercise some professional responsibility here when he senses what is happening. More likely is that he will resign from the account if he feels vulnerable or is removed if he starts to act responsibly. Note that I have never seen a notice of a trustee resignation or removal that gave a cause. This can be need-to-know information, but good luck with that.

Bank trustees' loyalty is first to themselves, next to the obligor who pay them their annual fees and then to the bondholders representing 25% or more of an issue. And don't expect any help from the bond issuing authority who are lending their name and provenance to the bonds. They will go out of their way to tell you that they have absolutely no liability on the bonds, which translates into also having no concern with how bad a bond issue is from inception.

Forbes

by Richard Lehmann

Aug 9, 2021

MSRB Announces New Board Members for Fiscal Year 2022.

Washington, DC – The Municipal Securities Rulemaking Board (MSRB) today announced four new members to serve on the governing board of the self-regulatory organization charged by Congress with protecting municipal securities investors, issuers and the public interest. The new members will serve four-year terms beginning October 1, 2021.

“We strive to build a Board that is diverse, inclusive and reflective of the wide variety of perspectives that contribute to the field of public finance,” said Caroline Cruise, Chair of the Board’s Nominating Committee. “This year’s class is outstanding, with a diversity of backgrounds and expertise that will make a lasting contribution to our market. My fellow Board members and I look forward to working alongside them to implement our new strategic plan and ensure our regulatory, transparency and data initiatives advance our long-term goal of strengthening market efficiency and transparency.”

New public members joining the MSRB Board in Fiscal Year 2022 are: Jennie Huang Bennett, Chief Financial Officer for the City of Chicago, and Katano Kasaine, Assistant General Manager and Chief Financial Officer at the Metropolitan Water District of Southern California. Joining the Board as regulated members are: Warren “Bo” Daniels, Atlanta-based Managing Director and Head of Public Finance of Loop Capital Markets, a minority-owned dealer firm based in Chicago, IL, and Liz Sweeney, President and founder of Nutshell Associates, LLC, a Maryland-based municipal advisory firm. The new Board members were selected from more than 60 applicants this year.

Congress established certain minimum requirements for Board composition, and all Board members are required to be individuals of integrity and knowledgeable of matters related to the municipal securities markets. The Board consists of four “classes” with staggered terms, with a new class elected annually in accordance with Congressional requirements and MSRB rules. Learn how the puzzle pieces come together to optimize representation on the Board.

For FY 2022, the Board will have 15 members, including eight independent public members and seven members from MSRB-regulated broker-dealers, banks and municipal advisors. The size of the Board was reduced as part of a series of governance enhancements that also tightened standards of independence for public members and established a lifetime service limit for Board members. To facilitate the transition to a smaller Board, the term of a current public member on the Board, Donna Simonetti, has been extended one year.

The MSRB recently announced that it has elected Patrick Brett, Managing Director and Head of Municipal Debt Capital Markets at Citi in New York, to serve as FY 2022 Chair of the Board. Meredith L. Hathorn, Managing Partner, Foley & Judell, L.L.P. in Baton Rouge, LA, will serve as Vice Chair.

New MSRB Board Members, Fiscal Year 2022

Jennie Huang Bennett is Chief Financial Officer for the City of Chicago, where she oversees financial strategy and policy and a $13 billion total budget, manages a $26 billion portfolio of City of Chicago debt, and directs financial policy for a number of City agencies, among other things. Prior to her service at the City, Ms. Bennett served as Chief Financial Officer for Chicago Public Schools. She began her career with Morgan Stanley’s Municipal Securities Division in New York and ultimately served as Executive Director in Chicago. Ms. Bennett has also served on the boards of directors of several organizations, including Perspective Charter Schools, Chicago Opera Theater

and Women in Public Finance. Ms. Bennett earned a bachelor's degree in political science and economics from the University of Pennsylvania.

Warren "Bo" Daniels is Managing Director and Head of Public Finance of Loop Capital Markets, a minority-owned firm based in Chicago, IL. He is based in Atlanta and has been the senior banker on over $45 billion of financings during his career and worked on numerous higher education, general obligation, sales tax, transportation, water and sewer, single/multi-family housing, and financial products transactions, as well as complex asset-backed and structured financings. He has extensive experience with sophisticated and complex financial products, hedges and variable rate products. Prior to joining Loop Capital Markets and establishing its Atlanta office, Mr. Daniels was responsible for running the Atlanta public finance office for PNC, Morgan Stanley's Atlanta office, and Goldman Sachs's Chicago office, having begun his career with Goldman Sachs in New York. Mr. Daniels earned a bachelor's degree from the University of Southern California and a Master of Business Administration from the Wharton School of the University of Pennsylvania.

Katano Kasaine is an Assistant General Manager and Chief Financial Officer at the Metropolitan Water District of Southern California. In this capacity, she is responsible for directing Metropolitan's financial activities, including accounting and financial reporting, debt issuance and management, financial planning and strategy, managing Metropolitan's investment portfolio, budget administration, financial analysis, financial systems, and developing rates and charges. Her municipal experience spans over 26 years. In her prior role as Director of Finance/Treasurer for the City of Oakland, Ms. Kasaine managed all aspects of the City's finance functions, including the issuance and administration of all debt financings, budgets, and financial reporting. She has served on various public boards and committees, including the Oakland Joint Powers Financing Authority, the Police and Fire Retirement System and the Deferred Compensation Committee. Ms. Kasaine earned a bachelor's degree in business administration from Dominican University and a master's degree in public health from Loma Linda University.

Liz Sweeney is President and founder of Nutshell Associates, LLC, a Maryland-based municipal advisory firm, where she provides public finance expertise, debt advisory, and analytical tools and data to lenders, investors, and borrowers to improve access to capital and informed business decisions. Ms. Sweeney also serves on the board of directors of the University of Maryland Medical System. In addition, as a member of the Standard Government Reporting Working Group, she provides subject-matter expertise and market education in support of the development and adoption of machine-readable data standards for municipal and nonprofit disclosure. She began her career as a rating analyst with S&P Global Ratings, ultimately leading credit policy and risk management initiatives as Managing Director and Criteria Officer. She earned a bachelor's degree in finance from Georgetown University and a Master of Business Administration from NYU Stern School of Business.

Date: August 4, 2021

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SIFMA Joint Trades Letter on the Adjustable Interest Rate (LIBOR) Act.

SUMMARY

SIFMA and joint trade associations provided comments to the Committee on Financial Services and Subcommittee on Investor Protection, Entrepreneurship and Capital Markets in support of the Adjustable Interest Rate (LIBOR) Act to address "tough legacy" contracts that currently reference LIBOR.

Read the Comment Letter.

SIFMA Supports Legislation Addressing Transition Away from LIBOR.

Washington, D.C., July 28, 2021 – SIFMA sent a letter to House Financial Services Committee Chairwoman Maxine Waters (D-CA) and Ranking Member Patrick McHenry (R-NC) expressing support for the Committee passing H.R. 4616, the Adjustable Interest Rate (LIBOR) Act, sponsored by Representative Brad Sherman (D-CA). SIFMA also looks forward to working with Congress on the legislation as the process goes forward.

"SIFMA supports H.R. 4616 because it addresses the variety of issues associated with the cessation of all tenors of U.S. dollar LIBOR and facilitates a smooth transition to alternative reference rates," said SIFMA president and CEO Kenneth E. Bentsen, Jr. "As a result of the discontinuation of LIBOR, trillions of dollars of contracts, securities, and loans that use LIBOR but lack adequate fallback language will be left outstanding. One specific subset, commonly referred to as 'tough legacy' contracts, has no clear path to amendment, thereby posing a significant risk to the financial system and the underlying borrowers and consumers, investors, and banks if such legislation is not passed. We thank Chair Waters, Chairman Sherman and members of the Committee for their work on this bill."

The letter further notes, "While the Alternative Reference Rates Committee (ARRC) has successfully developed language that was recently implemented in New York and Alabama, a variety of inconsistent, or non-existent, state legislation cannot provide the benefits of a uniform Federal law, including contract certainty, fairness and equality of outcomes, avoidance of years of litigation, and market liquidity. Such a patchwork could compromise the very intent to provide a smooth transition. The legislation would change the reference rate on certain financial contracts which reference LIBOR to the Secured Overnight Financing Rate (SOFR), or an appropriately adjusted form of SOFR. This will allow the contracts to continue to function as originally intended after LIBOR is discontinued, without the need to be amended or subject to litigation."

SIFMA also joined several other trade associations in sending a letter to Chairwoman Waters, Ranking Member McHenry, and Representatives Sherman and Huizenga which expresses broad industry support for H.R. 4616.

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MSRB Issues Guidance on Primary Offering Disclosure Form.

The MSRB issued a new FAQ to clarify the process for completing the MSRB's primary offering

disclosure form (i.e., Form G-32).

In the FAQ, the MSRB explains that:

- Blue Sky restrictions are not required to be identified as a Restriction on Issue;
- contractual restrictions on the sale, resale, or transfer of securities must be identified as a Restriction on Issue;
- an underwriter should provide the name of a deal participant who is acting in the role of a municipal advisor, even where a municipal advisor is identified by another term;
- the underwriter should identify municipal securities as having a credit enhancement when the form of credit enhancement does not fall into the categories of “letter of credit” or “bond insuranc e”;
- Form G-32 allows an underwriter to indicate that obligated person(s) for municipal securities are determined by objective criteria and may change; and
- underwriters are required to complete Form G-32 for municipal securities that are not eligible for the New Issue Information Dissemination Service.

Cadwalader Wickersham & Taft LLP

July 27 2021

Frequently Asked Questions About MSRB Form G-32.

The MSRB is providing the following set of responses to frequently asked questions (FAQs) to enhance understanding of the process for completing Form G-32.

These FAQs do not create new legal or regulatory requirements or new interpretations of existing requirements and should not be interpreted by regulated entities or examining authorities as establishing new standards of conduct. This resource has not been filed with the Securities and Exchange Commission (SEC) and has not been approved nor disapproved by the SEC. Regulated entities, examining authorities, and others should not interpret this resource as establishing new or additional obligations for any person.

This resource should be read in conjunction with MSRB Rule G-32 and all related rules and interpretations. The full text of MSRB rules and interpretations can be found at https://msrb.org/Rules-and-Interpretations/MSRB-Rules.

1. Restrictions on Issue

Form G-32 requires information regarding when a subsequent “sale, resale, or transfer” of a municipal security is subject to certain qualifying terms or conditions (a “Restriction on Issue”). An example of a Restriction on Issue could be that a sale, resale, or transfer of a municipal security is contingent on a prospective purchaser meeting a requisite level of sophistication, as may be evidenced by investor affirmations about the investor’s knowledge, experience, and capability to evaluate the merits and risks of the prospective purchase (e.g., similar or analogous affirmations as those of a ‘Qualified Institution Buyer’).

1.1 Would the state-by-state restrictions on the sale of certain municipal securities commonly referred to as “State Blue Sky Restrictions” need to be

identified on Form G-32's field regarding *Restriction on Issue*?"
No, State Blue Sky Restrictions do not need to be identified on Form G-32 as a *Restriction on Issue*.

1.2 Would the contractual restrictions on the sale, resale, or transfer of municipal securities that are typically incorporated into the transactional documents (e.g., on the bond certificate itself and/or in the bond indenture or trust agreement) need to be identified on Form G-32 in the *Restrictions on Issue* field?
Yes, Form G-32 is intended to capture these types of contractual restrictions on the sale, resale, or transfer of municipal securities. Underwriters who believe the *Restrictions on Issue* field is applicable should check the box to indicate yes, there are such contractual restrictions, as for example, in a primary offering structured to meet the exemption requirements of Rule 15c2-12(d)(1)(i) for purchase by thirty-five investors or less (as further described therein).

2. Additional Syndicate Managers

Form G-32 requires information regarding each of the other co-managers in a syndicate.

2.1 Who should be identified as a co-manager?
For purposes of the *Additional Syndicate Managers* field on Form G-32 and the determination of which firms should be identified as a senior manager or co-manager, an underwriter completing Form G-32 should identify all the other underwriting firms that it understands to be participating in the syndicate account's offering, sale, and distribution, such as, for example, those firms acting as underwriters and listed in a final pricing wire and/or by the issuer in a final official statement.

2.2 Must the underwriter identify selling group members?
No, for purposes of the *Additional Syndicate Managers* field on Form G-32, the MSRB does not expect an underwriter to identify selling group members.

3. Name of Municipal Advisor

Form G-32 requires information regarding the name of each municipal advisor.

3.1 If a municipal advisor firm is described in the issuer's official statement as a "financial advisor" should an underwriter provide the name of that firm as a municipal advisor in Form G-32?
Yes, an underwriter completing Form G-32 should provide the name of a deal participant who the underwriter understands to be acting in the role of a municipal advisor, even in instances where a municipal advisor may be identified by a different term, such as financial advisor, in an official statement or offering memorandum.

4. Credit Enhancers and LEIs

Form G-32 requires information regarding the legal entity identify or "LEI" for credit enhancers when such LEI is readily available.

4.1 For purposes of Form G-32, should the underwriter identify the municipal securities as having a credit enhancement when the form of credit enhancement does not fall into the category of a letter of credit nor bond insurance?
Yes, the *Credit Enhancement* section on Form G-32 indicates whether the municipal securities have a form of credit enhancement. In situations where the form of credit enhancement does not fall into the categories of "letter of credit" or "bond insurance," the underwriter can select the "other" option. An underwriter should select the "other" category when the offering includes a different form of credit enhancement. For example, state intercept programs,1 other guarantees (like a state guarantee), federal or state agency guarantees,2 and/or standby bond purchase agreements should be identified as " other."

4.2 Must the underwriter attempt to provide the LEI when a municipal entity, federal agency, or other similar public entity is the entity providing credit enhancement?
Yes, an underwriter should input LEI information for credit enhancers into the *Credit Enhancement* section of Form G-32 when such information is "readily available," in other words, easily obtainable via a general search on the internet. The underwriter should attempt to provide an LEI for entities providing a credit enhancement that falls into the " other" category (such as those credit enhancements described in the response to frequently asked question 4.1).

5. Obligated Persons and LEIs

Form G-32 requires information regarding the LEI for obligated persons (other than the issuer of the municipal securities) when such LEI is readily available.

5.1 Does Form G-32 allow for situations where obligated persons are subject to objective criteria and may change?
Yes, the *Obligated Persons* section of Form G-32 allows an underwriter to indicate that the obligated person(s) for the municipal securities are determined by objective criteria and may not be known at the time of issuance or may subsequently change in the future, such as in the case of certain pooled financings. Instances when an underwriter understands that obligated persons are subject to objective criteria (and so may change), and the official statement identifies the obligated person(s) who initially meet the stated objective criteria, then the underwriter should identify such obligated person(s) and indicate that the municipal securities are subject to objective criteria. Instances when an underwriter understands that obligated persons are subject to objective criteria (and so may change), but the official statement does not identify any such obligated persons, the underwriter need only indicate that the municipal securities are subject to objective criteria.

6. Private Placements

An underwriter must submit information about private placements on Form G-32, including when the municipal securities are not eligible for the New Issue Information Dissemination Service ("Non-NIIDS-Eligible Offerings").

6.1 Are underwriters required to complete Form G-32 for Non-NIIDS-Eligible

Offerings, like certain private placements?
Yes, underwriters are required to complete Form G-32 for Non-NIIDS-Eligible Offerings, like certain private placements. Effective as of August 2, 2021, for a Non-NIIDS-Eligible Offering, an underwriter would continue to be required to manually complete the same data fields that it currently completes on Form G-32, with the addition of three new data fields regarding: (i) the original minimum denomination, (ii) whether the original minimum denomination of the offering could change, and (iii) whether there is a Restriction on Issue. For purposes of Form G-32, the term "underwriter," as defined by reference in Rule G-32 to SEC Rule 15c2-12, encompasses certain dealers acting as agents in the private placements of municipal securities. See File No. SR-MSRB-2020-08 (Oct. 13, 2020), at note 12 .

7. Submission Timing

Rule G-32's submission requirements depend on whether the new issuance is a *NIIDS-Eligible Primary Offering or a Non-NIIDS-Eligible Primary Offering*. See Rule G-32(b)(i)(A)(1) and Rule G- 32 (b)(i)(A)(2), respectively. For *NIIDS-Eligible Offerings,* the information auto-populated into Form G-32 is sourced from information submitted by an underwriter to NIIDS pursuant to MSRB Rule G-34 (which governs the content and timing of submissions to NIIDS to facilitate the timely reporting, comparison, confirmation, and settlement of transactions in a new issue). See Rule G-34(a)(ii).

7.1 For advance refundings, when must the CUSIP(s) and dollar amount(s) of the refunded securities be submitted on Form G-32?
In a primary offering generating proceeds to advance refund previously issued municipal securities (i.e., "Advance Refunded Bonds"), Form G-32 requires information regarding the dollar amount of each of the Advance Refunded Bonds being advance refunded and CUSIP information for those Advance Refunded Bonds (when applicable). This information must be submitted on Form G-32 at the earlier of either (i) the date of official statement submission or (ii) the closing date. *(Added July 30, 2021)*

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1. The MSRB understands that it is common for municipal securities issued by school districts to include a credit enhancement mechanism by which public funds in support of school district activities are redirected to satisfy debt service shortfalls.

2. The MSRB understands that it is common for municipal securities issued by housing agencies to incorporate certain guarantees or insurance provided by other federal and/or state agencies, like Ginnie Mae, Fannie Mae, or Freddie Mac.

House Financial Services Committee July 2021 Markup: SIFMA Comment Letter

SUMMARY

SIFMA respectfully submits this letter to the House Financial Services Committee in connection with its full committee markup on July 28, 2021. Included are SIFMA's views on H.R. 4616, the

Adjustable Interest Rate (LIBOR) Act; H.R. 4617, to require the Securities and Exchange Commission to carry out a study on payment for order flow; H.R. 4618, the Short Sale Transparency and Market Fairness Act; H.R. 4619, to amend the Securities Exchange Act of 1934 to prohibit trading ahead by market makers, and for other purposes; H.R. 935, the Small Business Mergers, Acquisitions, Sales, and Brokerage Simplification Act; and H.R. 2265, the Financial Exploitation Prevention Act.

Read the Comment Letter.

GASB Issues Proposal to Enhance Concepts for Notes to Financial Statements.

Norwalk, CT, July 20, 2021 — The Governmental Accounting Standards Board (GASB) today issued a proposed Concepts Statement to guide the Board when establishing note disclosure requirements for state and local governments. The document is part of the GASB's response to the results of its research reexamining existing note disclosure requirements.

The proposed concepts primarily are intended to provide the GASB with criteria to consistently evaluate notes to financial statements in the standards-setting process. They also may help stakeholders to understand the fundamental concepts underlying future GASB pronouncements.

The Revised Exposure Draft (RED), *Communication Methods in General Purpose External Financial Reports That Contain Basic Financial Statements: Notes to Financial Statements*, proposes concepts such as:

- The purpose of notes to financial statements
- The intended users of note disclosures
- The types of information that should be disclosed in notes
- The types of information that are not appropriate for note disclosures.

A key element of the proposed Concepts Statement is the concept of essentiality. The RED would establish that notes to financial statements are essential to making economic, social, or political decisions or assessing accountability. The RED also identifies the characteristics that indicate information is essential to users:

- Users utilize the information in their analyses for making decisions or assessing accountability or would modify those analyses to incorporate the information if it were made available.
- The information has or would have a meaningful effect on users' analyses for making decisions or assessing accountability.
- A breadth or depth of users utilize or would utilize the information in their analyses for making decisions or assessing accountability.

The GASB issued an Exposure Draft (ED) on this topic in early 2020. The Board has issued this RED to incorporate feedback received from stakeholders on the previous ED and to seek feedback on the resulting proposed revisions, which the Board believes will improve the final concepts.

The Revised Exposure Draft is available for download at no charge on the GASB website, www.gasb.org. Stakeholders are encouraged to review and provide comments by October 15, 2021.

GASB Proposes Omnibus Statement Addressing Wide Range of Practice Issues.

Norwalk, CT, July 19, 2021 — The Governmental Accounting Standards Board (GASB) has proposed guidance addressing various accounting and financial reporting issues identified during the implementation and application of certain GASB pronouncements or during the due process on other pronouncements.

The issues covered by the Exposure Draft, *Omnibus 20xx*, include:

- Accounting and financial reporting for exchange or exchange-like financial guarantees
- Classification and reporting of certain derivative instruments that are neither hedging derivative instruments nor investment derivative instruments
- Clarification of certain provisions of:
- Statement No. 87, *Leases*
- Statement No. 94, *Public-Private and Public-Public Partnerships and Availability Payment Arrangements*
- Statement No. 96, *Subscription-Based Information Technology Arrangements*
- Extending the period during which the London Interbank Offered Rate (LIBOR) is considered an appropriate benchmark interest rate for the qualitative evaluation of the effectiveness of certain interest rate swaps
- Accounting for the distribution of benefits as part of the Supplemental Nutrition Assistance Program (SNAP)
- Disclosures related to nonmonetary transactions
- Pledges of future revenues when resources are not received by the pledging government
- Updating certain terminology for consistency with existing authoritative standards.

The Exposure Draft is available on the GASB website, www.gasb.org. The GASB invites stakeholders to review the proposal and provide comments by September 17, 2021.

07/19/21

MSRB Holds Quarterly Board Meeting and Elects New Officers.

Washington, DC – The municipal market's self-regulatory organization held its quarterly Board of Directors meeting in Washington, DC, on July 21-22, 2021. The Municipal Securities Rulemaking Board (MSRB) elected new officers and adopted a new organizational vision, long-term strategic direction and supporting budget for Fiscal Year 2022 that will advance its mission in the upcoming fiscal year and beyond.

Also at its meeting, the Board considered and advanced several market regulation initiatives, received updates on multi-year technology and data activities, and authorized staff to prepare a request for information on Environmental, Social and Governance (ESG) considerations in the municipal market.

Board Leadership

The Board announced today that it has elected Patrick Brett, Managing Director and Head of

Municipal Debt Capital Markets at Citi in New York, to serve as FY 2022 Chair of the Board. Meredith L. Hathorn, Managing Partner, Foley & Judell, L.L.P. in Baton Rouge, LA, will serve as Vice Chair. Officer terms are one year. The Board will soon announce the incoming class of four new Board members whose terms will begin October 1, 2021.

“Both Patrick and Meredith exemplify the commitment to public service and market knowledge that are hallmarks of great Board leaders,” said MSRB CEO Mark Kim. “I am delighted to be working alongside Patrick and Meredith to advance the MSRB’s bold new strategic plan grounded in our Congressional mandate to protect investors, issuers and the public interest.”

Strategic Planning

The Board defined the MSRB’s mission, vision and values and adopted a long-term strategic plan aimed at strengthening market efficiency and transparency. The MSRB will publish its strategic plan for the next four years in advance of the new fiscal year, which begins on October 1, 2021.

“We spent the last year listening to our stakeholders and formulating the Board’s vision for the market that helps bring progress and opportunity to communities across the country,” Kim said. “I’m looking forward to continuing that dialogue and sharing our strategy for how we can deploy the tools of regulation, technology and data in impactful ways to serve the public interest.”

Market Regulation

The Board advanced the following initiatives through the rulemaking process:

- **Filing proposed amendments to MSRB Rule G-10:** After considering comments received during its public request for comment, the Board determined to seek approval from the Securities and Exchange Commission (SEC) of a proposed rule change to streamline the delivery of disclosures to investors and to amend Rule G-48 to exempt sophisticated municipal market professionals (SMMPs) from the disclosure requirement.
- **Filing proposed modernization of MSRB Rule G-34:** Based on stakeholder feedback, the Board authorized staff to seek SEC approval of proposed amendments to align the text of the MSRB’s rule on obtaining CUSIP numbers with current market practices.
- **Additional comment on draft solicitor municipal advisor rule:** The Board discussed comments received on a public request for comment on draft MSRB Rule G-46 and determined to publish a second request for comment on a revised draft rule addressing feedback from commenters.
- **Filing proposed amendments on the application of Regulation Best Interest:** The MSRB will seek SEC approval of proposed amendments to MSRB rules to apply aspects of the SEC’s Regulation Best Interest requirements to bank dealers. The MSRB also will seek approval to amend Rule G-48 to address changes to the responsibility to perform a quantitative suitability analysis when making a recommendation to certain SMMPs.

The MSRB plans to advance these rulemaking initiatives over the next several months. Previously, the Board authorized staff to issue a request for comment on next steps in modernizing MSRB Rule G-27 on dealer supervision, which the MSRB plans to do later this summer for a 90-day comment period.

Professional Qualifications and Compliance

The Board received an update on the implementation of the Series 54 examination for municipal advisor principals. Municipal advisor principals must take and pass the exam by November 12, 2021.

On November 13, 2021, issuers and the public may view a listing of individuals who have become qualified with the Series 54 exam. View the MSRB's Series 54 resource page.

The Board also discussed the development of compliance resources for dealers and municipal advisors. The Board's FY 2021 Compliance Advisory Group helps identify those areas where compliance assistance is warranted and will be most impactful.

Technology and Data

The Board continues to monitor efforts to leverage cloud technology to modernize the MSRB's critical market transparency systems, including the Electronic Municipal Market Access (EMMA®) website. The Board also previewed a prototype data quality dashboard that is being developed to enhance the MSRB's data governance and oversight capabilities.

"As our market becomes increasingly data-driven, we recognize that enhancing data quality will significantly enhance the ability of market participants to make informed decisions," Kim said.

ESG Initiatives in the Municipal Market

The Board continues to discuss how ESG considerations are influencing market practices and has authorized staff to prepare a draft request for information from the public. The request for information would be intended to inform the MSRB's understanding of this evolving area in the market and how the MSRB might approach ESG trends in the context of its mission to protect investors, municipal issuers, and the public interest.

MSRB Budget and Operations

The Board approved a $43 million operating budget for FY 2022, reflecting a 4% increase over FY 2021. The Board also approved designating an additional $7.5 million of organizational reserves to increase the Board's Designated Systems Modernization Fund, bringing the total level of funding for this multi-year effort to $17.5 million to modernize the MSRB's suite of market transparency technology systems. The full budget will be published this fall.

The MSRB today is announcing that it has named Omer Ahmed as Chief Financial Officer to oversee the budget and financial stewardship of the organization. Ahmed previously served as Chief Risk Officer. Nanette Lawson, who has been serving in the dual capacity of Chief Operating Officer and CFO, will focus exclusively on COO responsibilities, including management of the MSRB's regulatory, technology and data divisions as well as finance, risk, human resources and administration.

More information regarding the Board's governance, membership, and Committees and advisory groups is available at https://www.msrb.org/About-MSRB/Governance/MSRB-Board-of-Directors.

Date: July 23, 2021

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SECF Fines UBS $10m Over Alleged Adviser 'Misdirection' of Investments.

The US Securities and Exchange Commission today (20 July) fined UBS Financial Services Inc more than $10m over charges that its financial advisers misdirected certain exchange-traded products to retail investors.

According to the SEC's order, over a four-year period, UBS improperly allocated bonds intended for retail customers to parties known in the industry as "flippers," who then immediately resold or "flipped" the bonds to other broker-dealers at a profit.

The order found that UBS registered representatives knew or should have known that flippers were not eligible for retail priority.

In addition, the order finds that UBS registered representatives facilitated over 2,000 trades with flippers, which allowed UBS to obtain bonds for its own inventory, thereby circumventing the priority of orders set by the issuers and improperly obtaining a higher priority in the bond allocation process.

"Retail order periods are intended to prioritize retail investors' access to municipal bonds and we will continue to pursue violations that undermine this priority," said LeeAnn G. Gaunt, chief of the Division of Enforcement's Public Finance Abuse Unit.

The SEC previously brought charges of municipal bond offering "flipping" and retail order period abuses in August 2018, in December 2018, in September 2019, and in April 2020.

Without admitting or denying the findings, UBS consented to a cease-and-desist order that finds it violated the disclosure, fair dealing, and supervisory provisions of Municipal Securities Rulemaking Board Rules G-11(k), G-17, and G-27, and also failed reasonably to supervise within the meaning of Section 15(b)(4)(E) of the Securities Exchange Act of 1934.

The order imposed a $1.75m penalty, $6.74m in disgorgement of ill-gotten gains plus over $1.5m in prejudgment interest, and a censure.

In related actions, the SEC instituted settled proceedings today against UBS registered representatives William S. Costas and John J. Marvin.

The SEC's order found that Costas and Marvin negligently submitted retail orders for municipal bonds on behalf of their flipper customers and that Costas also helped UBS bond traders improperly obtain bonds for UBS's own inventory through his flipper customer.

internationalinvestment.net

by Mark Battersby

July 2021

Economists Find Underreporting of Municipalities' Private Debt Obligations.

The underreporting of bank debt remains a sizable risk for holders of municipal bonds two years after Securities and Exchange Commission rule changes designed to improve transparency.

That was the conclusion of scholarly research performed by three economists and presented Monday at the Brookings Municipal Finance Conference. The paper authored by Federal Reserve Board

economists Ivan Ivanov and Nathan Heinrich, as well as by Tom Zimmermann of the University of Cologne, examined the effectiveness of regulations designed to improve the transparency of private debt and concluded the requirements have limited effectiveness.

“We need to worry about it,” Ivanov said during a webcast presentation of the research. “We need to be able as a market to observe these.”

Roughly 50% of issuers are now required to disclose private debt under the 2019 amendments to the SEC?s Rule 15c2-12, the researchers found. Those rules require disclosure of the incurrence of a financial obligation of the issuer or obligated person, if material, as well as any agreement to covenants, events of default, remedies, priority rights, or other similar terms of a financial obligation of the issuer or obligated person, if these are material.

Bond investors need to be aware of other obligations because such debts could potentially impair bondholders, particularly if the debt is explicitly senior to the outstanding bonds.

The authors used subscription services and confidential data, and also hand-collected information from over 2,300 filing documents. In each filing, they searched for the obligation amount, interest rate and maturity, noting whether the filing was new or amending an existing obligation, and whether the filing included a term sheet summarizing the obligation.

The authors found that private debt was significantly underreported, using their data to determine when a filing was required and whether an associated disclosure appeared on EMMA.

“In the vast majority of bank loan events where disclosure is required, the associated issuer makes no disclosure on the EMMA system,” the researchers discovered. “For example, out of the 4,813 such bank loan events, only 935 events corresponding to 156 entities are associated with mandatory disclosures filings on the EMMA system.”

Further, the authors found, there was a wide range in the quality of these disclosures, with most offering up the size of the obligation but many excluding important information about the terms of such obligations.

The economists suggested that low issuer sophistication and familiarity with 15c2-12 might partly explain the underreporting.

Emily Brock, the director of the federal liaison center at the Government Finance Officers Association also noted during the conference that some issuers might not be aware of the rule. Brock said there is an opportunity for the whole muni market to improve the state of disclosure.

“We can use this opportunity to see what EMMA can be,” Brock said.

She also said it’s important to note that issuers lean heavily on counsel to help them make the determination about materiality, a concept that can be difficult to pin down. The SEC has generally declined to elaborate on when an obligation or event is material, not wanting to go beyond the Supreme Court?s ruling that something is material if there is “a substantial likelihood” that the disclosure would have been viewed by a “reasonable investor” as having significantly altered the “total mix of information” used to make an investment decision.

The Brookings conference continues through Wednesday.

By Kyle Glazier

BY SOURCEMEDIA | MUNICIPAL | 07/13/21 01:18 PM EDT

Why There's Rising Interest in Giving More Updates to Bondholders.

Investors and others would like to see more timely information about developments with municipal borrowers' finances. "Voluntary disclosure" can help, experts say.

When state and local governments borrow through the municipal bond market to pay for road construction, waterworks upgrades or other projects, they take on obligations to report information about their finances to investors until the debt is paid off.

But issuers often don't release annual financial statements they're required to disclose until well after their fiscal year ends, making it hard to get an up to date picture about what's happening with their finances. This gap between budget cycles and these disclosure filings can stretch six or even nine months and some investors and others think the delay is too long.

Beyond the annual financial reports, under Securities and Exchange Commission rules, borrowers also have to publicly file ongoing notices about certain events, like delinquent payments, unscheduled draws on debt service reserves, or credit ratings changes.

In recent years, there's been growing interest in what's known as "voluntary disclosure," where state and local governments proactively release information related to their finances and relevant for investors, even though they are under no obligation to do so.

"Voluntary disclosure is taking it a step further and truly is what it sounds like. It's voluntary," said David Erdman, Wisconsin's capital finance director, during a Government Finance Officers Association conference taking place online through next week.

Erdman pointed out that after a state or local government finishes issuing bonds and the proceeds are in-hand and construction is underway on a project, it can feel as though the deal is done. But until the bonds are paid off, that's not really the case.

While the bonds are still outstanding, investors might be looking to assess the value of the debt, or to sell it on the "secondary market." But infrequent financial disclosures by governments mean the official information they have to make decisions can be incomplete or scarce.

Erdman likens the situation here to someone trying to buy a used car, who can only find information about the vehicle that's a year or more old. "You wouldn't know what the current miles are, you wouldn't know if there's any recent accidents," he said.

"Same thing goes with a municipal bond," Erdman added, "more information needs to be out there and that's where voluntary information kicks in."

A good example of when disclosures to investors like this can make sense is the Covid-19 pandemic, which stirred historic uncertainty about state and local governments' finances, the expenses they were taking on to respond to the crisis, and how it was affecting revenues.

There are other situations as well. For instance, a cyberattack, or a natural disaster like a flood or hurricane, might be the kind of event that investors want more details about to have a better understanding of how it's affecting a bond issuer's finances.

GFOA points out that going beyond disclosure requirements can be a part of investor relations programs and is one measure that state and local bond issuers can take to promote efficiency in the municipal bond market and to improve how their debt sales are received.

“In today’s municipal market there is a heightened focus on the quality and transparency of disclosure practices by issuers,” GFOA notes.

Presenting information in context

Jacquelynne Jennings, a partner at the law firm Schiff Hardin LLP (emphasizing she was speaking for herself and not the company) said that the SEC has shown an interest in greater financial disclosures by municipal borrowers.

“They would like for municipalities to more mirror the corporate markets and provide information quarterly, which is not going to happen, but at least more frequently than annually,” she said.

Erdman said he’s concerned that if municipalities and others don’t ramp up disclosure efforts, the SEC might push additional regulations on the muni market—possibly to a degree that some issuers might turn to bank loans rather than bonds to meet their capital needs.

That said, for governments that only sell bonds every few years, voluntary disclosures may not be worth the effort. “The state of Wisconsin is a large, frequent issuer and there’s probably some investor relations benefit for us doing this,” Erdman said.

But even for medium size issuers, who are issuing bonds on an annual basis, he added, providing voluntary information to the market on a regular basis can have benefits.

Also, voluntary disclosure doesn’t have to just be for bad news. It can highlight notable developments that have to do with things like revenue growth or infusions of federal funds.

Another area where voluntary disclosure can make sense is around issues that have to do with environmental, social and governance, or ESG, criteria. GFOA describes these factors as areas that can affect a community’s long-term sustainability. Examples include things like exposure to climate risks, demographic changes, or pension liabilities.

“ESG is all the rage right now in the market,” said Timothy Ewell, chief assistant county administrator for Contra Costa County, California. “In California, wildfires are the thing now.” He noted that a GFOA’s committee is working to assemble best practices and templates that jurisdictions can use to disclose ESG information to the bond market.

Jennings discussed how if finance officials fall short sharing timely information with bond market participants, investors may look elsewhere to assess what’s going on and that could mean turning to statements by politicians or press reports that don’t give a full picture.

“A lot of times doing this voluntary disclosure is the best chance that you have,” she said, “to present the facts in their proper context.”

ROUTE FIFTY

by BILL LUCIA

JULY 15, 2021

Insurance Commissioner, Acting as Liquidator of RRG, Is Not a "Governmental Authority."

When is an insurance commissioner not a governmental authority? A federal district judge reminds us that a state insurance commissioner, when acting as receiver of an insolvent insurer, acts in a different capacity to his governmental role. This principle can cause an insurance commissioner to fall outside a contractual definition of "governmental authority" even where the definition contains inclusive language on multiple capacities.

In a decision handed down on June 21, 2021, in *Trinidad Navarro, Insurance Commissioner of Delaware v. Allied World Surplus Lines Insurance Company*, Judge Kari A. Dooley of the U.S. District Court for Connecticut held that a claim made by Commissioner Navarro as liquidator of a risk retention group (RRG) was not a "governmental claim" within the meaning of an insurance policy. According to the court, the commissioner was acting as a "private receiver" for the insurer's benefit. (The court did not distinguish between an RRG and an insurer.) Assuming it is not reversed or overturned, the decision could provide new guidance to future litigants in disputes over the nature and scope of insurance receiverships.

Carrier Solutions Risk Retention Group, Inc. (CSRRG) was a Delaware-domiciled RRG managed by service provider USA Risk Group (West) Inc. (USA Risk). In 2010, facing insolvency, CSRRG was placed in liquidation proceedings by Delaware chancery court in accordance with Delaware's statutory insurance insolvency scheme, with the then-Delaware commissioner appointed as liquidator. (Navarro became commissioner after his 2016 election.)

USA Risk was insured against professional liability risks under an Allied World Surplus Lines Insurance Company (Allied World) policy. The policy imposed distinct limits of liability for ordinary " claims" against USA Risk on the one hand, and "governmental claims" on the other, defined as a claim or investigation (in pertinent part) "brought by any federal, state or municipal agency, insurance department or other governmental or quasi-governmental authority, in any capacity, whether in its own right, on behalf of an individual or entity, or by an individual or entity on the agency's or authority's behalf."

In May 2012, the Delaware commissioner as receiver sued USA Risk alleging that USA Risk had caused or contributed to CSRRG's insolvency. USA Risk submitted a claim to Allied World under the professional liability policy. After bearing USA Risk's litigation expenses for about three years in the case brought by the receiver, around July 2015 Allied World withdrew its defense and contended that it had satisfied its $25,000 limit of liability applicable to "governmental claims." In response, the receiver took the position that his claim was not a "governmental claim" and thus eligible for the policy's more generous policy limit of $3,000,000.

CSRRG and USA Risk settled their litigation for $1,000,000. CSRRG thereupon, as USA Risk's assignee, sued Allied World in federal district court in Connecticut, where Allied World (and a predecessor insurer that had issued the policy initially) had administrative offices. CSRRG sought to recover damages arising from Allied World's failure to continue its defense of the claim after around July 2015. Allied World moved to dismiss the case on the grounds that the receiver's claim against USA Risk constituted a "governmental claim" under the Allied World policy and that, therefore, Allied World was liable for no more than $25,000.

Allied World argued that the insurance commissioner is a governmental authority and therefore, CSRRG's claim against Allied World categorically is a "governmental claim." The commissioner, in

turn, argued that he was acting not in his capacity as government official but rather as a "private receiver" on behalf of CSRRG. (The commissioner also argued in the alternative that, even if the claim would otherwise be classified as a governmental claim, an exclusion in the definition, for claims by a governmental authority in its role as a customer, would not apply. The court explained that it did not need to reach this question because it was holding that the "governmental claim" definition was unavailing in the first place.)

According to the court, the law of Vermont (where the policy was issued) and the law of Connecticut would not differ on the interpretive question before it. Therefore the court found it unnecessary to specify which state's law governed. (The court also analyzed Delaware case law in its opinion, without stating expressly that Delaware law controlled.) While noting possible ambiguity in the policy's definition of "governmental claim," the court explained that neither the commissioner nor Allied World was arguing that the policy language was ambiguous. The court would make an interpretive ruling based solely on the language itself.

Judge Dooley explained that she found the commissioner's position (that he is not a governmental authority in this instance) "persuasive." CSRRG's liquidation order issued by the Delaware chancery court had vested in the commissioner all rights and interests in all of CSRRG's property and empowered the commissioner to act generally on behalf of CSRRG for the benefit of its members, policyholders, creditors and other stakeholders. The commissioner's action against Allied World was functionally an action by a private party, CSRRG.

The court did not cite any previous insurance policy or other contract that had been so interpreted in a judicial forum and did not invoke any other textual predicate for its decision. The court relied mainly on decisions by state courts, including Delaware courts, holding more generally or in other contexts that an insurance commissioner acts in two different capacities. For example, Judge Dooley cited a New York case in which the state insurance liquidation bureau (an arm of the insurance department) was immune from state audits of government bodies. A Pennsylvania case was cited for the proposition that a regulator's prior actions qua regulator could not be asserted against her as an affirmative defense in an action brought by her as receiver. A Kentucky court had held that the commissioner as receiver fell outside the state's open public records act.

The court rejected the commissioner's argument concerning the allegedly plain language of the policy ("any . . . governmental or quasi-governmental authority, in any capacity. . . ." (emphasis added)) and the commissioner's exclusive role as receiver. In other words, the commissioner was contending that he is the only official authorized by law to act as receiver, and therefore the policy's use of the term "in any capacity" must capture this role. The court held that, on the contrary, the term "governmental claim" must exclude the receiver's capacity. The court did not explain its specific basis for construing "in any capacity" to mean, in essence, something less than all possible capacities.

Whether *Navarro* will change how insurance receivers are perceived by the courts in contractual situations involving terms such as "governmental authority" remains to be seen. For the time being, it does seem as though Judge Dooley has broken at least some new ground in explaining that an insurance policy's definition of "governmental claim," even where referring to any capacity of a governmental body, must categorically exclude a commissioner's statutory and exclusive role as a receiver.

Kramer Levin Naftalis & Frankel LLP – Daniel A. Rabinowitz

July 15 2021

Broker-Dealer Settles FINRA Charges for Systemic Supervisory Failures.

A broker-dealer settled FINRA charges for systemic failures, including failing to establish (i) a reasonable supervisory system for its mutual fund and municipal bond businesses, and (ii) a reasonable system of supervisory controls to verify its surveillance systems.

In a Letter of Acceptance, Waiver and Consent, FINRA found that the firm's automated surveillance system, which identified and flagged for review Class A Share switches, did not provide the critical data needed to evaluate the suitability of a transaction, such as the holding periods of the Class A Shares. FINRA found that the firm allowed its supervisors to clear alerts that were missing information significant to a suitability determination after obtaining an explanation from the registered representative but without further investigation.

FINRA also found that the firm (i) did not address suitability reviews specific to municipal bonds in its written supervisory procedures and (ii) failed to conduct a heightened review of a broker's short-term trading of Puerto Rican municipal bonds, which carried additional risks due to the restructuring of Puerto Rican debt. As a result, the firm violated FINRA Rule 3110 ("Supervision") and MSRB Rules G-27(b) and (c).

With regard to supervisory controls, FINRA stated, the firm's annual tests did not examine whether the system for supervising two active business lines (mutual funds and municipal bonds) was reasonably designed to achieve compliance with FINRA and MSRB suitability rules, in violation of FINRA Rule 3120 ("Supervisory Control System") and MSRB Rule G-27(f).

The above-mentioned conduct is also a violation of FINRA Rule 2010 ("Standards of Commercial Honor and Principles of Trade").

To settle the charges, the firm agreed to (i) a censure, (ii) a $750,000 fine (including $225,000 for the MSRB Rule G-27 violations) and (iii) an undertaking to certify the implemented supervisory systems.

Cadwalader Wickersham & Taft LLP

July 14 2021

Municipal Advisor Principal Qualification Exam: MSRB Reminder

Municipal advisor firms must ensure their municipal advisor principals are properly qualified.

The November 12, 2021 compliance deadline to take and pass the Municipal Advisor Principal Qualification (Series 54) Exam is approaching.

Learn more.

National Public Finance Guarantee Corporation, et al. v. UBS Financial

Services Inc., et al: SIFMA Amicus Brief

Court:
Puerto Rico Appeals Court

Amicus Issue:
Whether plaintiffs claim that they reasonably relied upon the due diligence conducted by underwriters, where underwriters included standard industry disclaimers to the effect that underwriters do not guarantee the accuracy or completeness of the information in the offering documents, can survive a motion to dismiss.

Counsel of Record:
Orrick, Herrington & Sutcliffe LLP

- Richard A. Jacobsen
- Daniel A. Rubens
- Siobhan Atkins

Read the SIFMA Amicus Brief.

NFMA White Paper on Guidance & Insights Regarding Emergency Event Disclosure Affecting State & Local Governments: COVID-19 Focus

White Paper on Guidance & Insights Regarding Emergency Event Disclosure Affecting State & Local Governments: COVID-19 Focus Released

- White paper, dated June 2021
- Press release, dated July 6, 2020

Amendments to Rule G-10 Notification Requirement for Dealers: SIFMA Comments

SUMMARY

SIFMA provides comments to the Municipal Securities Rulemaking Board (MSRB) on their Notice 2021-08, proposing an amendment to MSRB Rule G-10, on investor and municipal advisory client education and protection, to clarify the requirements for brokers, dealers, and municipal securities dealers to provide the annual notifications to those customers who would be best served by receipt of the annual notifications.

Read the SIFMA comments.

BDA Supports Proposed Changes to MSRB Rule G-10

Yesterday, BDA submitted a comment letter to the MSRB on Notice 2021-08, “Request for Comment

on Amendments to Rule G-10 Notification Requirements for Dealers." MSRB last month issued the Notice and proposed to amend MSRB Rule G-10. Rule G-10 requires municipal dealers to send certain annual information disclosures to investor customers and issuer clients.

View the comment letter here.

In our January letter on MSRB strategic priorities, BDA pointed out that Rule G-10 requires municipal-related disclosures to customers who have never and may never own or trade municipal security. We requested that the MSRB amend Rule G-10 to target required disclosures to municipal securities customers. Notice 2021-08 represents the MSRB's action on this issue.

In our letter, **we support the MSRB's proposal**. We also request three additional changes to Rule G-10 to exempt issuers from these disclosures, permit clearing firms to transmit the relevant disclosures on behalf of their introducing firms' customers, and require disclosures for customers who own municipal securities or have traded them since the last annual disclosure rather than owned municipals at any time in the last year.

Bond Dealers of America

June 29, 2021
